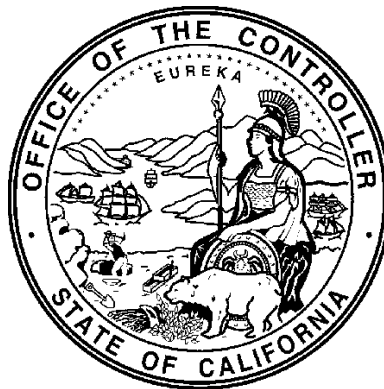


STATE OF CALIFORNIA

**UNAUDITED
BASIC FINANCIAL
STATEMENTS**

For the Year Ended
June 30, 2005



*Prepared by
The Office of the State Controller*

STEVE WESTLY
California State Controller

Contents

UNAUDITED BASIC FINANCIAL STATEMENTS

GOVERNMENT-WIDE FINANCIAL STATEMENTS

Statement of Net Assets.....	4
Statement of Activities.....	6

FUND FINANCIAL STATEMENTS

Balance Sheet – Governmental Funds.....	10
Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Assets.....	11
Statement of Revenues, Expenditures, and Changes in Fund Balances – Governmental Funds.....	12
Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances of Governmental Funds to the Statement of Activities.....	13
Statement of Net Assets – Proprietary Funds.....	14
Statement of Revenues, Expenses, and Changes in Fund Net Assets – Proprietary Funds.....	18
Statement of Cash Flows – Proprietary Funds.....	20
Statement of Fiduciary Net Assets – Fiduciary Funds and Similar Component Units.....	24
Statement of Changes in Fiduciary Net Assets – Fiduciary Funds and Similar Component Units.....	25

DISCRETELY PRESENTED COMPONENT UNITS

FINANCIAL STATEMENTS


Statement of Net Assets – Discretely Presented Component Units – Enterprise Activity.....	28
Statement of Revenues, Expenses, and Changes in Fund Net Assets – Discretely Presented Component Units – Enterprise Activity.....	30

NOTES TO THE FINANCIAL STATEMENTS

Notes to the Financial Statements – Index.....	31
Notes to the Financial Statements.....	35

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Basic Financial Statements



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Government-wide Financial Statements



Statement of Net Assets

June 30, 2005

(amounts in thousands)

	Primary Government			
	Governmental	Business-type		Component
	Activities	Activities	Total	Units
ASSETS				
Current assets:				
Cash and pooled investments	\$ 20,132,043	\$ 4,936,560	\$ 25,068,603	\$ 1,979,076
Amount on deposit with U.S. Treasury	—	1,872,214	1,872,214	—
Investments	1,026,003	1,032,405	2,058,408	13,589,618
Restricted assets:				
Cash and pooled investments	—	1,768,812	1,768,812	2,818
Investments	—	—	—	31,227
Due from other governments	—	62,434	62,434	—
Receivables (net)	9,546,742	443,706	9,990,448	3,062,330
Internal balances	315,184	(315,184)	—	—
Due from primary government	—	—	—	201,033
Due from other governments	8,487,290	186,977	8,674,267	845,267
Prepaid items	35,988	7,921	43,909	4,020
Inventories	90,114	21,970	112,084	124,113
Recoverable power costs (net)	—	573,000	573,000	—
Other current assets	278,072	9,968	288,040	151,513
Total current assets	39,911,436	10,600,783	50,512,219	19,991,015
Noncurrent assets:				
Restricted assets:				
Cash and pooled investments	—	1,934,393	1,934,393	144,203
Investments	—	89,171	89,171	37,473
Loans receivable	—	627,588	627,588	—
Investments	—	2,154,461	2,154,461	28,921,009
Net investment in direct financing leases	—	5,386,207	5,386,207	—
Receivables (net)	1,097,109	43,357	1,140,466	857,079
Loans receivable	1,896,306	3,029,435	4,925,741	5,541,969
Recoverable power costs (net)	—	7,356,000	7,356,000	—
Deferred charges	188,842	1,435,768	1,624,610	72,388
Capital assets:				
Land	14,730,050	45,782	14,775,832	598,297
State highway infrastructure	55,114,882	—	55,114,882	—
Collections – nondepreciable	19,354	—	19,354	250,445
Buildings and other depreciable property	19,687,916	7,998,397	27,686,313	23,530,232
Less: accumulated depreciation	(8,002,315)	(3,246,357)	(11,248,672)	(10,943,488)
Construction in progress	5,628,463	1,612,665	7,241,128	3,359,432
Other noncurrent assets	—	3,668	3,668	340,862
Total noncurrent assets	90,360,607	28,470,535	118,831,142	52,709,901
Total assets	\$ 130,272,043	\$ 39,071,318	\$ 169,343,361	\$ 72,700,916

	Primary Government			Component
	Governmental	Business-type		Units
	Activities	Activities	Total	
LIABILITIES				
Current liabilities:				
Accounts payable	\$ 12,377,530	\$ 546,592	\$ 12,924,122	\$ 1,820,885
Due to component units	175,380	25,653	201,033	—
Due to other governments	7,191,541	94,762	7,286,303	242,756
Dividends payable	—	—	—	3,100
Deferred revenue	1,713	51,214	52,927	670,279
Tax overpayments	4,378,724	—	4,378,724	—
Deposits	89,910	3,890	93,800	450,953
Contracts and notes payable	41,677	—	41,677	12,818
Advance collections	633,634	31,834	665,468	312,844
Interest payable	756,696	201,230	957,926	115,996
Securities lending obligations	—	—	—	3,792,663
Benefits payable	—	369,198	369,198	3,029,110
Current portion of long-term obligations	3,321,589	1,656,999	4,978,588	2,557,333
Other current liabilities	836,923	68,272	905,195	1,698,667
Total current liabilities	29,805,317	3,049,644	32,854,961	14,707,404
Noncurrent liabilities:				
Loans payable	1,011,800	—	1,011,800	9,078
Benefits payable	—	16,591	16,591	13,695,492
Lottery prizes and annuities	—	1,764,169	1,764,169	—
Compensated absences payable	1,708,392	32,444	1,740,836	249,121
Certificates of participation, commercial paper, and other borrowings	246,501	51,093	297,594	233,120
Capital lease obligations	3,687,955	—	3,687,955	1,934,900
General obligation bonds payable	43,820,067	1,963,305	45,783,372	—
Revenue bonds payable	7,977,700	22,013,523	29,991,223	11,842,941
Other noncurrent liabilities	7,585,807	542,406	8,128,213	1,617,219
Total noncurrent liabilities	66,038,222	26,383,531	92,421,753	29,581,871
Total liabilities	95,843,539	29,433,175	125,276,714	44,289,275
NET ASSETS				
Investment in capital assets, net of related debt	79,579,676	1,155,342	80,735,018	8,734,425
Restricted:				
Nonexpendable – endowments	—	—	—	2,724,209
Expendable:				
Endowments and gifts	—	—	—	5,726,228
Business and transportation	1,470,593	219,109	1,689,702	1,484,455
Resources	1,736,074	—	1,736,074	—
Health and human services	1,117,768	1,743,654	2,861,422	—
Education	1,594,975	4,134,133	5,729,108	1,407,929
General government	1,628,324	475,614	2,103,938	148,582
Unemployment programs	83,323	662,863	746,186	—
Workers' compensation liability	—	—	—	2,863,419
Total expendable	7,631,057	7,235,373	14,866,430	11,630,613
Unrestricted	(52,782,229)	1,247,428	(51,534,801)	5,322,394
Total net assets	34,428,504	9,638,143	44,066,647	28,411,641
Total liabilities and net assets	\$ 130,272,043	\$ 39,071,318	\$ 169,343,361	\$ 72,700,916

Statement of Activities

Year Ended June 30, 2005

(amounts in thousands)

FUNCTIONS/PROGRAMS	Expenses	Program Revenues		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
Primary government				
Governmental activities:				
General government	\$ 8,781,281	\$ 4,754,711	\$ 1,244,056	\$ —
Education	53,280,047	2,936,693	5,867,154	—
Health and human services	62,022,255	3,280,970	31,196,152	—
Resources	4,168,445	1,934,532	219,463	—
State and consumer services	1,041,468	601,322	6,052	—
Business and transportation	7,157,847	2,541,072	2,501,651	1,090,419
Correctional programs	6,630,482	12,354	100,913	—
Tax relief	2,157,280	1,784	—	—
Interest on long-term debt	2,408,246	—	—	—
Total governmental activities	147,647,351	16,063,438	41,135,441	1,090,419
Business-type activities:				
Electric Power	5,655,000	5,655,000	—	—
Water Resources	731,393	750,282	—	—
Public Building Construction	299,900	315,718	—	—
State Lottery	3,493,984	3,512,126	—	—
Unemployment Programs	8,939,654	10,459,688	—	—
High Technology Education	33,690	36,737	—	—
Toll Facilities	20,861	66	—	—
State University Dormitory Building				
Maintenance and Equipment	449,080	395,396	—	—
State Water Pollution Control Revolving	14,638	55,218	—	73,182
Housing Loan	142,085	121,063	—	—
Other enterprise programs	86,612	115,901	—	—
Total business-type activities	19,866,897	21,417,195	—	73,182
Total primary government	\$ 167,514,248	\$ 37,480,633	\$ 41,135,441	\$ 1,163,601
Component units:				
University of California	\$ 19,259,070	\$ 12,944,815	\$ 3,976,549	\$ —
State Compensation Insurance Fund	7,623,551	8,456,280	—	—
California Housing Finance Agency	488,859	436,001	122,958	—
Public Employees' Benefit Fund	3,553,260	3,023,329	—	—
Nonmajor component units	1,882,325	1,219,683	466,927	—
Total component units	\$ 32,807,065	\$ 26,080,108	\$ 4,566,434	\$ —

General revenues:

Personal income taxes	
Sales and use taxes	
Corporation taxes	
Insurance taxes	
Other taxes	
Investment and interest	
Escheat	
Miscellaneous	

Transfers

Nonoperating grants and gifts

Total general and other revenues and transfers

Change in net assets

Net assets, July 1, 2004
Net assets, June 30, 2005

* Restated

Net (Expenses) Revenues and Changes in Net Assets			
Primary Government			
Governmental Activities	Business-type Activities	Total	Component Units
\$ (2,782,514)		\$ (2,782,514)	
(44,476,200)		(44,476,200)	
(27,545,133)		(27,545,133)	
(2,014,450)		(2,014,450)	
(434,094)		(434,094)	
(1,024,705)		(1,024,705)	
(6,517,215)		(6,517,215)	
(2,155,496)		(2,155,496)	
(2,408,246)		(2,408,246)	
<u>(89,358,053)</u>		<u>(89,358,053)</u>	
	\$ —	\$ —	
	18,889	18,889	
	15,818	15,818	
	18,142	18,142	
	1,520,034	1,520,034	
	3,047	3,047	
	(20,795)	(20,795)	
	(53,684)	(53,684)	
	113,762	113,762	
	(21,022)	(21,022)	
	29,289	29,289	
	1,623,480	1,623,480	
<u>(89,358,053)</u>	<u>1,623,480</u>	<u>(87,734,573)</u>	
			\$ (2,337,706)
			832,729
			70,100
			(529,931)
			(195,715)
			<u>(2,160,523)</u>
42,504,352	—	42,504,352	—
32,488,563	—	32,488,563	—
11,174,937	—	11,174,937	—
2,231,060	—	2,231,060	—
2,507,729	—	2,507,729	—
289,363	—	289,363	—
525,897	—	525,897	—
(23,340)	—	(23,340)	—
27,727	(27,727)	—	—
—	—	—	4,039,615
<u>91,726,288</u>	<u>(27,727)</u>	<u>91,698,561</u>	<u>4,039,615</u>
2,368,235	1,595,753	3,963,988	1,879,092
32,060,269 *	8,042,390	40,102,659	26,532,549 *
<u>\$ 34,428,504</u>	<u>\$ 9,638,143</u>	<u>\$ 44,066,647</u>	<u>\$ 28,411,641</u>

The notes to the financial statements are an integral part of this statement.

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Fund Financial Statements



Balance Sheet

Governmental Funds

June 30, 2005

(amounts in thousands)

	General	Federal	Transportation Construction	Nonmajor Governmental	Total
ASSETS					
Cash and pooled investments	\$ 8,108,829	\$ 282,145	\$ 2,013,104	\$ 9,223,047	\$ 19,627,125
Investments	—	—	—	1,026,003	1,026,003
Receivables (net)	7,773,506	6,530	396,117	1,286,861	9,463,014
Due from other funds	764,966	85	1,129,475	2,521,467	4,415,993
Due from other governments	790,391	7,617,328	1,733	66,104	8,475,556
Interfund receivables	151,979	—	628,900	2,263,668	3,044,547
Loans receivable	101,003	41,735	—	1,619,267	1,762,005
Other assets	43,028	—	92,663	108,151	243,842
Total assets	\$ 17,733,702	\$ 7,947,823	\$ 4,261,992	\$ 18,114,568	\$ 48,058,085
LIABILITIES					
Accounts payable	\$ 1,221,511	\$ 1,308,016	\$ 136,975	\$ 2,745,086	\$ 5,411,588
Due to other funds	5,255,222	4,862,075	36,449	535,901	10,689,647
Due to component units	140,274	—	—	30,322	170,596
Due to other governments	2,816,133	1,663,490	137,823	2,574,095	7,191,541
Deferred revenue	—	—	—	1,713	1,713
Interfund payables	3,280,311	—	—	642,749	3,923,060
Tax overpayments	4,371,094	—	—	7,630	4,378,724
Deposits	7,216	—	11,699	67,345	86,260
Contracts and notes payable	—	—	—	30,142	30,142
Advance collections	29,580	59,890	5,176	365,546	460,192
Interest payable	5,457	10,439	28,615	33,319	77,830
Other liabilities	486,221	16,885	219,341	601,421	1,323,868
Total liabilities	17,613,019	7,920,795	576,078	7,635,269	33,745,161
FUND BALANCES					
Reserved for:					
Encumbrances	540,382	—	2,302,979	3,496,628	6,339,989
Interfund receivables	151,979	—	628,900	2,263,668	3,044,547
Loans receivable	101,003	41,735	—	1,562,793	1,705,531
Continuing appropriations	803,721	—	2,321,717	2,249,471	5,374,909
Unreserved, reported in:					
General Fund	(1,476,402)	—	—	—	(1,476,402)
Special revenue funds	—	(14,707)	(1,567,682)	1,309,845	(272,544)
Capital projects funds	—	—	—	(403,106)	(403,106)
Total fund balances (deficits)	120,683	27,028	3,685,914	10,479,299	14,312,924
Total liabilities and fund balances	\$ 17,733,702	\$ 7,947,823	\$ 4,261,992	\$ 18,114,568	

Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Assets

(amounts in thousands)

Total fund balances – governmental funds	\$ 14,312,924
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Amounts reported for governmental activities in the Statement of Net Assets are different because:

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.	86,762,631
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Other long-term assets are not available to pay for current-period expenditures and, therefore, are not reported.	1,097,109
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Internal service funds are used by management to charge the costs of certain activities, such as fleet management and management information systems, to individual funds. The assets and liabilities of the internal service funds are included in governmental activities in the Statement of Net Assets.	615,634
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Deferred bond issue costs, discounts, and premiums are reported as current expenditures in the funds. However, deferred issue costs and net discounts are amortized over the life of the bonds and are included in the governmental activities in the Statement of Net Assets.	188,842
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General obligation bonds totaling \$46,220,283 and revenue bonds totaling \$8,068,980 are not due and payable in the current period and, therefore, are not reported in the funds.	(54,289,263)
--	--------------

Certain long-term liabilities are not due and payable in the current period and, therefore, adjustments to these liabilities are not reported in the funds:

Compensated absences adjustments	(1,666,440)
Certificates of participation and commercial paper adjustments	(752,013)
Capital lease adjustments	(3,913,473)
Other long-term obligations	(7,927,447)

(14,259,373)

Net assets of governmental activities	\$ 34,428,504
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Statement of Revenues, Expenditures, and Changes in Fund Balances

Governmental Funds

Year Ended June 30, 2005

(amounts in thousands)

	General	Federal	Transportation Construction	Nonmajor Governmental	Total
REVENUES					
Personal income taxes	\$ 42,424,929	\$ —	\$ —	\$ 170,423	\$ 42,595,352
Sales and use taxes	25,782,760	—	2,517,734	4,014,748	32,315,242
Corporation taxes	11,191,937	—	—	—	11,191,937
Insurance taxes	2,231,060	—	—	—	2,231,060
Other taxes	778,172	—	—	1,704,163	2,482,335
Intergovernmental	—	41,134,952	—	1,798,429	42,933,381
Licenses and permits	42,328	—	906,203	4,005,494	4,954,025
Charges for services	127,607	—	120,627	700,913	949,147
Fees	172,059	—	—	4,521,057	4,693,116
Penalties	54,673	489	—	640,054	695,216
Investment and interest	241,824	—	44,268	290,005	576,097
Escheat	525,897	—	—	—	525,897
Other	707,684	—	92,992	2,954,750	3,755,426
Total revenues	84,280,930	41,135,441	3,681,824	20,800,036	149,898,231
EXPENDITURES					
Current:					
General government	2,259,495	1,065,042	16,104	5,170,841	8,511,482
Education	40,942,687	6,565,389	980	4,799,897	52,308,953
Health and human services	24,810,689	29,840,305	—	7,364,634	62,015,628
Resources	858,262	215,144	6	3,003,690	4,077,102
State and consumer services	493,037	6,166	—	474,263	973,466
Business and transportation	12,428	2,443,778	3,485,312	2,616,096	8,557,614
Correctional programs	6,622,819	33,124	—	2,671	6,658,614
Tax relief	949,428	—	—	1,186,830	2,136,258
Capital outlay	414,738	—	113,004	1,119,412	1,647,154
Debt service:					
Bond and commercial paper retirement	1,346,146	41,545	5,000	2,279,428	3,672,119
Interest and fiscal charges	1,724,313	23,589	57,820	438,042	2,243,764
Total expenditures	80,434,042	40,234,082	3,678,226	28,455,804	152,802,154
Excess (deficiency) of revenues over (under) expenditures	3,846,888	901,359	3,598	(7,655,768)	(2,903,923)
OTHER FINANCING SOURCES (USES)					
General obligation bonds and commercial paper issued	—	—	80,000	4,978,339	5,058,339
Revenue bonds issued	—	—	—	99,250	99,250
Refunding bonds issued	—	—	5,470	1,931,960	1,937,430
Payment to refunding agent	—	—	(5,470)	(1,931,960)	(1,937,430)
Capital leases	414,738	—	—	—	414,738
Transfers in	406,591	—	10,628	4,162,982	4,580,201
Transfers out	(3,006,834)	(929,990)	(52,504)	(557,464)	(4,546,792)
Total other financing sources (uses) ..	(2,185,505)	(929,990)	38,124	8,683,107	5,605,736
Net change in fund balances	1,661,383	(28,631)	41,722	1,027,339	2,701,813
Fund balances (deficits), July 1, 2004	(1,540,700)	55,659	3,644,192	9,451,960 *	11,611,111
Fund balances, June 30, 2005	\$ 120,683	\$ 27,028	\$ 3,685,914	\$ 10,479,299	\$ 14,312,924

* Restated

Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances of Governmental Funds to the Statement of Activities

(amounts in thousands)

Net change in fund balances – total governmental funds	\$ 2,701,813
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Amounts reported for governmental activities in the Statement of Activities are different because:

Governmental funds report capital outlays as expenditures. However, in the Statement of Activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which capital outlays exceed depreciation in the current period.	1,975,646
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Revenues in the Statement of Activities that do not provide current financial resources are deferred and not reported as revenues in the funds.	203,627
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Bonds and other noncurrent financing instruments provide current financial resources to governmental funds in the form of debt, which increases long-term liabilities in the Statement of Net Assets. Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the Statement of Net Assets. The following amounts represent the difference between proceeds and repayments.

General obligation bond adjustments	(1,782,419)	
Revenue bond adjustments	32,875	
Certificates of participation and commercial paper adjustments	97,347	(1,652,197)

Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.

Compensated absences	(182,020)	
Lease adjustments	(177,437)	
Other long-term obligations	(502,236)	(861,693)

Internal service funds are used by management to charge the costs of certain activities, such as fleet management and management information systems, to individual funds. The net revenue (expense) of the internal service funds is reported with governmental activities.	1,039
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Change in net assets of governmental activities	\$ 2,368,235
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Statement of Net Assets

Proprietary Funds

June 30, 2005

(amounts in thousands)

	Electric Power	Water Resources
ASSETS		
Current assets:		
Cash and pooled investments	\$ —	\$ 226,090
Amount on deposit with U.S. Treasury	—	—
Investments	650,000	—
Restricted assets:		
Cash and pooled investments	1,387,000	—
Due from other governments	—	—
Receivables (net)	—	96,697
Due from other funds	26,000	3,060
Due from other governments	—	7,208
Prepaid items	—	—
Inventories	—	9,953
Recoverable power costs (net)	573,000	—
Other current assets	—	3
Total current assets	<u>2,636,000</u>	<u>343,011</u>
Noncurrent assets:		
Restricted assets:		
Cash and pooled investments	1,482,000	156,912
Investments	—	50,862
Loans receivable	—	—
Investments	—	—
Net investment in direct financing leases	—	—
Receivables	—	—
Interfund receivables	—	91,517
Loans receivable	—	28,384
Recoverable power costs (net)	7,356,000	—
Deferred charges	—	1,320,903
Capital assets:		
Land	—	—
Buildings and other depreciable property	—	4,560,047
Less: accumulated depreciation	—	(1,644,113)
Construction in progress	—	72,950
Other noncurrent assets	—	—
Total noncurrent assets	<u>8,838,000</u>	<u>4,637,462</u>
Total assets	<u>\$ 11,474,000</u>	<u>\$ 4,980,473</u>

Business-type Activities – Enterprise Funds					Governmental Activities
Public Building Construction	State Lottery	Unemployment Programs	Nonmajor Enterprise	Total	Internal Service Funds
\$ —	\$ 326,645	\$ 2,534,182	\$ 1,849,643	\$ 4,936,560	\$ 504,927
—	—	1,872,214	—	1,872,214	—
—	354,997	—	27,408	1,032,405	—
262,468	—	—	119,344	1,768,812	—
—	—	—	62,434	62,434	—
127,542	152,718	143,264	59,285	579,506	81,255
17,539	3,675	20,199	8,391	78,864	307,103
—	—	93,125	86,644	186,977	11,734
—	6,790	—	1,131	7,921	35,988
—	8,199	—	3,818	21,970	90,114
—	—	—	—	573,000	—
—	—	—	9,965	9,968	27
407,549	853,024	4,662,984	2,228,063	11,130,631	1,031,148
266,692	—	—	28,789	1,934,393	—
—	—	—	38,309	89,171	—
—	—	—	627,588	627,588	—
—	2,032,158	—	122,303	2,154,461	—
5,020,898	—	—	365,309	5,386,207	—
—	—	43,357	—	43,357	—
—	—	—	9,400	100,917	—
—	—	—	3,001,051	3,029,435	—
—	—	—	—	7,356,000	—
65,346	21,944	—	27,575	1,435,768	—
—	4,923	—	40,859	45,782	231
—	73,625	14,203	3,350,522	7,998,397	1,250,088
—	(37,580)	(4,821)	(1,559,843)	(3,246,357)	(838,033)
1,185,720	—	—	353,995	1,612,665	3,433
—	—	—	3,668	3,668	—
6,538,656	2,095,070	52,739	6,409,525	28,571,452	415,719
\$ 6,946,205	\$ 2,948,094	\$ 4,715,723	\$ 8,637,588	\$ 39,702,083	\$ 1,446,867

(continued)

Statement of Net Assets (continued)

Proprietary Funds

June 30, 2005

(amounts in thousands)

	Electric Power	Water Resources
LIABILITIES		
Current liabilities:		
Accounts payable	\$ 424,000	\$ 48,206
Due to other funds	—	50,639
Due to component units	—	—
Due to other governments	—	73,430
Deferred revenue	—	—
Deposits	—	—
Contracts and notes payable	—	—
Advance collections	—	—
Interest payable	68,000	20,709
Benefits payable	—	—
Current portion of long-term obligations	453,000	115,420
Other current liabilities	—	—
Total current liabilities	<u>945,000</u>	<u>308,404</u>
Noncurrent liabilities:		
Interfund payables	—	—
Benefits payable	—	—
Lottery prizes and annuities	—	—
Compensated absences payable	—	—
Certificates of participation, commercial paper, and other borrowings	—	12,398
Capital lease obligations	—	—
General obligation bonds payable	—	683,715
Revenue bonds payable	10,529,000	2,369,741
Other noncurrent liabilities	—	400,784
Total noncurrent liabilities	<u>10,529,000</u>	<u>3,466,638</u>
Total liabilities	<u>11,474,000</u>	<u>3,775,042</u>
NET ASSETS		
Investment in capital assets, net of related debt	—	210,933
Restricted – Expendable:		
Construction	—	994,498
Debt service	—	—
Security for revenue bonds	—	—
Lottery	—	—
Unemployment program	—	—
Other purposes	—	—
Total expendable	—	994,498
Unrestricted	—	—
Total net assets	<u>—</u>	<u>1,205,431</u>
Total liabilities and net assets	<u>\$ 11,474,000</u>	<u>\$ 4,980,473</u>

Business-type Activities – Enterprise Funds					Governmental Activities
Public Building Construction	State Lottery	Unemployment Programs	Nonmajor Enterprise	Total	Internal Service Funds
\$ 4,692	\$ 36,193	\$ 7	\$ 27,365	\$ 540,463	\$ 177,995
33,423	279,759	202,824	67,120	633,765	270,160
25,653	—	—	—	25,653	4,784
539	—	11,841	8,952	94,762	—
—	—	—	51,214	51,214	—
—	—	—	3,890	3,890	3,650
—	—	—	—	—	11,535
24,636	2,882	—	4,316	31,834	173,442
63,366	—	—	49,155	201,230	—
—	—	369,198	—	369,198	—
340,252	582,496	—	165,831	1,656,999	18,610
—	—	66,847	1,425	68,272	4,475
492,561	901,330	650,717	379,268	3,677,280	664,651
—	—	—	3,129	3,129	96,774
—	—	—	16,591	16,591	—
—	1,764,169	—	—	1,764,169	—
—	4,903	8,122	19,419	32,444	41,952
—	—	—	38,695	51,093	—
—	—	—	—	—	3,991
—	—	—	1,279,590	1,963,305	—
6,357,041	—	—	2,757,741	22,013,523	—
—	1,785	—	139,837	542,406	23,865
6,357,041	1,770,857	8,122	4,255,002	26,386,660	166,582
6,849,602	2,672,187	658,839	4,634,270	30,063,940	831,233
—	40,968	9,317	894,124	1,155,342	424,469
74,920	—	—	352,525	1,421,943	—
21,683	—	—	206,463	228,146	—
—	—	—	690,022	690,022	—
—	275,907	—	—	275,907	—
—	—	4,047,567	—	4,047,567	—
—	—	—	571,788	571,788	—
96,603	275,907	4,047,567	1,820,798	7,235,373	—
—	(40,968)	—	1,288,396	1,247,428	191,165
96,603	275,907	4,056,884	4,003,318	9,638,143	615,634
\$ 6,946,205	\$ 2,948,094	\$ 4,715,723	\$ 8,637,588	\$ 39,702,083	\$ 1,446,867

(concluded)

Statement of Revenues, Expenses, and Changes in Fund Net Assets

Proprietary Funds

Year Ended June 30, 2005

(amounts in thousands)

	Electric Power	Water Resources
OPERATING REVENUES		
Unemployment and disability insurance	\$ —	\$ —
Lottery ticket sales	—	—
Power sales	4,714,000	104,521
Student tuition and fees	—	—
Services and sales	—	645,761
Investment and interest	—	—
Rent	—	—
Other	—	—
Total operating revenues	4,714,000	750,282
OPERATING EXPENSES		
Lottery prizes	—	—
Power purchases (net of recoverable power costs)	4,658,000	196,023
Personal services	—	183,096
Supplies	—	—
Services and charges	56,000	121,941
Depreciation	—	77,321
Distributions to beneficiaries	—	—
Interest expense	—	—
Amortization of deferred charges	—	—
Other	—	—
Total operating expenses	4,714,000	578,381
Operating income (loss)	—	171,901
NONOPERATING REVENUES (EXPENSES)		
Investment and interest income	941,000	—
Interest expense and fiscal charges	(941,000)	(152,847)
Lottery payments for education	—	—
Other	—	(165)
Total nonoperating revenues (expenses)	—	(153,012)
Income (loss) before contributions and transfers	—	18,889
Capital contributions	—	—
Transfers in	—	—
Transfers out	—	—
Change in net assets	—	18,889
Total net assets, July 1, 2004	—	1,186,542
Total net assets, June 30, 2005	\$ —	\$ 1,205,431

Business-type Activities – Enterprise Funds					Governmental Activities
Public Building Construction	State Lottery	Unemployment Programs	Nonmajor Enterprise	Total	Internal Service Funds
\$ —	\$ —	\$ 10,208,175	\$ —	\$ 10,208,175	\$ —
—	3,333,621	—	—	3,333,621	—
—	—	—	—	4,818,521	—
—	—	—	372,636	372,636	—
—	—	147,938	88,016	881,715	2,078,087
12,921	—	—	166,875	179,796	190
302,245	—	—	56,846	359,091	—
552	—	—	8,607	9,159	—
315,718	3,333,621	10,356,113	692,980	20,162,714	2,078,277
—	1,795,254	—	—	1,795,254	—
—	—	—	—	4,854,023	—
—	41,913	123,242	153,414	501,665	650,181
—	16,103	—	—	16,103	9,725
13,837	335,222	66,683	197,254	790,937	1,319,175
—	7,107	453	87,269	172,150	85,690
—	—	8,749,276	—	8,749,276	—
279,474	—	—	196,853	476,327	1,058
6,589	96	—	274	6,959	—
—	—	—	72,778	72,778	—
299,900	2,195,695	8,939,654	707,842	17,435,472	2,065,829
15,818	1,137,926	1,416,459	(14,862)	2,727,242	12,448
—	177,534	103,575	31,401	1,253,510	3,233
—	(149,514)	—	(10,424)	(1,253,785)	(5)
—	(1,148,775)	—	—	(1,148,775)	—
—	971	—	(28,700)	(27,894)	(3,692)
—	(1,119,784)	103,575	(7,723)	(1,176,944)	(464)
15,818	18,142	1,520,034	(22,585)	1,550,298	11,984
—	—	—	73,182	73,182	—
462	—	12,180	3,408	16,050	—
—	—	—	(43,777)	(43,777)	(10,945)
16,280	18,142	1,532,214	10,228	1,595,753	1,039
80,323	257,765	2,524,670	3,993,090	8,042,390	614,595
\$ 96,603	\$ 275,907	\$ 4,056,884	\$ 4,003,318	\$ 9,638,143	\$ 615,634

Statement of Cash Flows

Proprietary Funds

Year Ended June 30, 2005

(amounts in thousands)

	Electric Power	Water Resources
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from customers/employers	\$ 2,869,000	\$ 712,327
Receipts from interfund services provided	—	—
Payments to suppliers	(5,046,000)	(312,564)
Payments to employees	—	(183,095)
Payments for interfund services used	—	—
Payments for Lottery prizes	—	—
Claims paid to other than employees	—	—
Other receipts (payments)	1,651,000	—
Net cash provided by (used in) operating activities	(526,000)	216,668
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Changes in interfund payables and loans payable	—	—
Proceeds from revenue bonds	—	—
Retirement of general obligation bonds	—	—
Retirement of revenue bonds	(388,000)	—
Interest paid on operating debt	(480,000)	—
Transfers in	—	—
Transfers out	—	—
Grants received	—	—
Lottery payments for education	—	—
Other	847,000	(14,589)
Net cash provided by (used in) noncapital financing activities	(21,000)	(14,589)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Changes in interfund payables and loans payable	—	—
Acquisition of intangible assets	—	—
Acquisition of capital assets	—	(35,881)
Proceeds from sale of capital assets	—	—
Proceeds from notes payable and commercial paper	—	15,556
Principal paid on notes payable and commercial paper	—	(13,677)
Payment of capital lease obligations	—	—
Retirement of general obligation bonds	—	(46,320)
Proceeds from revenue bonds	—	278,647
Retirement of revenue bonds	—	(303,302)
Interest paid	—	(153,080)
Contributed capital	—	—
Net cash provided by (used in) capital and related financing activities	—	(258,057)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of investments	(50,000)	—
Proceeds from maturity and sale of investments	—	—
Change in interfund receivables and loans receivable	—	4,597
Earnings on investments	85,000	11,092
Net cash provided by (used in) investing activities	35,000	15,689
Net increase (decrease) in cash and pooled investments	(512,000)	(40,289)
Cash and pooled investments at July 1, 2004	3,381,000	423,291
Cash and pooled investments at June 30, 2005	\$ 2,869,000	\$ 383,002

Business-type Activities – Enterprise Funds					Governmental
Public Building	State	Unemployment	Nonmajor		Activities
Construction	Lottery	Programs	Enterprise	Total	Internal
					Service Funds
\$ 554,106	\$ 3,332,789	\$ 10,329,578	\$ 572,347	\$ 18,370,147	\$ 2,029,547
—	—	—	917	917	25,967
(13,515)	(94,642)	(66,693)	(261,652)	(5,795,066)	(1,378,710)
—	(36,287)	(122,984)	(157,161)	(499,527)	(578,458)
—	(8,542)	—	(124,643)	(133,185)	(100,436)
—	(2,031,748)	—	—	(2,031,748)	—
—	(233,496)	(8,735,198)	(236)	(8,968,930)	(10,084)
(276,873)	929	83,822	(147,003)	1,311,875	102,150
263,718	929,003	1,488,525	(117,431)	2,254,483	89,976
—	—	—	22	22	(901)
—	—	—	162,600	162,600	—
—	—	—	(2,500)	(2,500)	—
—	—	—	(309,270)	(697,270)	—
—	—	—	(12,117)	(492,117)	—
462	—	12,180	3,987	16,629	—
—	—	—	(20,150)	(20,150)	(10,946)
—	—	—	72,123	72,123	—
—	(1,134,756)	—	—	(1,134,756)	—
—	—	—	(54,000)	778,411	(3,382)
462	(1,134,756)	12,180	(159,305)	(1,317,008)	(15,229)
11,451	—	—	—	11,451	—
—	—	—	—	—	(2,463)
(720,396)	(10,974)	(4,801)	21	(772,031)	(25,360)
—	39	100	—	139	(12,760)
—	—	—	—	15,556	—
—	—	—	—	(13,677)	(2,471)
—	—	—	—	—	(2,930)
—	—	—	—	(46,320)	—
955,860	—	—	542,990	1,777,497	—
(290,210)	—	—	(290,195)	(883,707)	—
—	—	—	—	(153,080)	(1,063)
—	—	—	—	—	—
(43,295)	(10,935)	(4,701)	252,816	(64,172)	(47,047)
—	(92,847)	(464,689)	—	(607,536)	—
—	360,862	—	46,259	407,121	—
—	—	—	—	4,597	—
—	7,927	103,576	11,625	219,220	3,309
—	275,942	(361,113)	57,884	23,402	3,309
220,885	59,254	1,134,891	33,964	896,705	31,009
308,275	267,391	1,399,291	1,963,812	7,743,060	473,918
\$ 529,160	\$ 326,645	\$ 2,534,182	\$ 1,997,776	\$ 8,639,765	\$ 504,927

(continued)

Statement of Cash Flows (continued)

Proprietary Funds

Year Ended June 30, 2005

(amounts in thousands)

	<div>Electric Power</div>		<div>Water Resources</div>	
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES				
Operating income (loss)	\$	—	\$	171,901
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:				
Interest expense on operating debt		—		—
Depreciation		—		77,321
Accretion of capital appreciation bonds		—		—
Provisions and allowances		—		—
Accrual of deferred charges		—		—
Amortization of discounts		—		—
Amortization of deferred charges		—		(20,559)
Other		—		—
Change in assets and liabilities:				
Receivables		—		(10,048)
Due from other funds		—		—
Due from other governments		—		—
Prepaid items		—		—
Inventories		—		274
Net investment in direct financing leases		—		—
Recoverable power costs (net)		72,000		—
Other current assets		—		833
Loans receivable		—		—
Interfund receivable		—		—
Accounts payable		(28,000)		9,081
Due to other funds		—		15,998
Due to component units		—		—
Due to other governments		—		(29,088)
Deposits		—		—
Advance collections		—		—
Interest payable		—		—
Other current liabilities		(570,000)		—
Interfund payables		—		—
Deferred revenue		—		—
Benefits payable		—		—
Lottery prizes and annuities		—		—
Compensated absences payable		—		955
Other noncurrent liabilities		—		—
Total adjustments		(526,000)		44,767
Net cash provided by (used in) operating activities	\$	(526,000)	\$	216,668
Noncash capital and related financing and investing activities				
Interest accreted on annuitized prizes	\$	—	\$	—
Unclaimed Lottery prizes directly transferred to Education Fund		—		—
Unrealized loss on investment		—		—
Gain on investment		—		—
Loans Receivable contributed		—		—

Business-type Activities – Enterprise Funds						Activities
Public Building Construction	State Lottery	Unemployment Programs	Nonmajor Enterprise	Total		Internal Service Funds
\$ 15,818	\$ 1,137,926	\$ 1,416,459	\$ (14,862)	\$ 2,727,242	\$	12,448
—	—	—	—	—		1,058
—	7,107	453	87,269	172,150		85,690
2,536	—	—	3,613	6,149		—
—	1,891	—	(416)	1,475		—
(8,015)	—	—	—	(8,015)		—
(5,815)	—	—	—	(5,815)		—
6,589	96	—	(239)	(14,113)		—
(1,020)	1,906	—	1,510	2,396		3,410
—	(3,499)	10,613	(11,809)	(14,743)		(43,761)
(11,317)	397	5,766	(9,781)	(14,935)		(6,707)
—	—	(35,869)	(1,041)	(36,910)		(10,771)
—	—	—	284	284		(6,457)
—	58	—	(109)	223		8,068
261,269	—	—	24,638	285,907		—
—	—	—	—	72,000		—
—	5,694	—	(5,847)	680		1,445
—	—	—	(35,734)	(35,734)		—
—	—	(5,223)	43	(5,180)		—
1,046	13,337	7	(23,251)	(27,780)		(13,031)
279	145	83,288	(15,773)	83,937		77,321
2,070	—	(1,123)	—	947		2,756
—	—	—	(2,289)	(31,377)		(311)
—	(4)	—	(1,079)	(1,083)		2,075
(46)	—	—	(9,699)	(9,745)		(41,977)
324	—	—	2,384	2,708		—
—	777	3,670	(18,679)	(584,232)		7,088
—	—	—	(243)	(243)		—
—	—	—	(12,283)	(12,283)		—
—	(334)	15,191	1,842	16,699		—
—	(236,494)	—	—	(236,494)		—
—	—	257	(19,508)	(18,296)		11,111
—	—	(4,964)	(56,372)	(61,336)		521
247,900	(208,923)	72,066	(102,569)	(472,759)		77,528
\$ 263,718	\$ 929,003	\$ 1,488,525	\$ (117,431)	\$ 2,254,483	\$	89,976
(concluded)						
\$ —	\$ 149,515	\$ —	\$ —	\$ 149,515	\$	—
—	27,019	—	—	27,019		—
—	18,142	—	—	18,142		—
—	—	—	116,957	116,957		—
—	—	—	2,243	2,243		—

The notes to the financial statements are an integral part of this statement.

Statement of Fiduciary Net Assets

Fiduciary Funds and Similar Component Units

June 30, 2005

(amounts in thousands)

	Private Purpose Trust	Pension and Other Employee Benefit Trust	Investment Trust Local Agency Investment	Agency
ASSETS				
Cash and pooled investments	\$ 22,444	\$ 1,600,961	\$ 18,662,977	\$ 4,059,624
Investments, at fair value:				
Short-term	—	5,649,059	—	—
Equity securities	—	227,060,642	—	—
Debt securities	—	105,963,056	—	—
Real estate	—	18,204,480	—	—
Alternative	1,721,860	24,746,264	—	—
Securities lending collateral	—	69,652,234	—	—
Total investments	1,721,860	451,275,735	—	—
Receivables (net)	2,653	12,362,985	43,059	676,047
Due from other funds	64,096	438,038	—	6,292,183
Due from other governments	—	—	—	14,726
Prepaid Items	—	—	—	17,946
Interfund receivables	1,011,800	—	—	—
Loans receivable	—	—	—	145,429
Other assets	99,995	2,784,569	—	362
Total assets	2,922,848	468,462,288	18,706,036	\$ 11,206,317
LIABILITIES				
Accounts payable	7,573	9,051,667	36	\$ 3,768,146
Due to other funds	64	2,355	286	—
Due to other governments	—	624	133,901	5,824,880
Tax overpayments	—	—	—	229
Benefits payable	—	1,428,282	—	—
Deposits	99,995	—	—	737,950
Advance collections	—	—	—	101,182
Securities lending obligations	—	69,649,742	—	—
Interfund payables	—	—	—	134,301
Other liabilities	1,091,716	9,251,993	—	639,629
Total liabilities	1,199,348	89,384,663	134,223	\$ 11,206,317
NET ASSETS				
Held in trust for pension benefits, pool participants, and other purposes	<u>\$ 1,723,500</u>	<u>\$ 379,077,625</u>	<u>\$ 18,571,813</u>	

Statement of Changes in Fiduciary Net Assets

Fiduciary Funds and Similar Component Units

Year Ended June 30, 2005

(amounts in thousands)

	Private Purpose Trust	Pension and Other Employee Benefit Trust	Investment Trust Local Agency Investment
ADDITIONS			
Contributions:			
Employer	\$ —	\$ 9,321,959	\$ —
Plan member	—	6,810,668	—
Total contributions	—	16,132,627	—
Investment income:			
Net appreciation in fair value of investments	—	29,617,995	—
Interest, dividends, and other investment income	49,376	14,996,717	431,339
Less: investment expense	—	(3,514,948)	—
Net investment income	49,376	41,099,764	431,339
Receipts from depositors	364,418	—	22,523,859
Transfers in	4,229	1,034	—
Other	40,757	4,578	—
Total additions	458,780	57,238,003	22,955,198
DEDUCTIONS			
Distributions paid and payable to participants	—	15,818,451	429,731
Refunds of contributions	—	885,920	—
Administrative expense	7,569	348,309	1,608
Payments to and for depositors	148,139	347,057	25,902,751
Total deductions	155,708	17,399,737	26,334,090
Change in net assets	303,072	39,838,266	(3,378,892)
Net assets, July 1, 2004	1,420,428	339,239,359	21,950,705
Net assets, June 30, 2005	\$ 1,723,500	\$ 379,077,625	\$ 18,571,813

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Discretely Presented Component Units Financial Statements



Statement of Net Assets

Discretely Presented Component Units – Enterprise Activity

June 30, 2005

(amounts in thousands)

	University of California	State Compensation Insurance	California Housing Finance Agency	Public Employees' Benefits	Nonmajor Component Units	Total
ASSETS						
Current assets:						
Cash and pooled investments	\$ 244,126	\$ 306,211	\$ 740,754	\$ 1,874	\$ 686,111	\$ 1,979,076
Investments	6,369,050	2,240,563	2,613,536	2,179,457	187,012	13,589,618
Restricted assets:						
Cash and pooled investments	—	—	—	—	2,818	2,818
Investments	—	—	—	—	31,227	31,227
Receivables (net)	1,394,064	1,042,964	342,793	1,599	280,910	3,062,330
Due from primary government	196,232	—	—	3,627	1,174	201,033
Due from other governments	675,499	—	—	118,082	51,686	845,267
Prepaid items	—	2,355	651	—	1,014	4,020
Inventories	123,829	—	—	—	284	124,113
Other current assets	98,498	457	76	—	52,482	151,513
Total current assets	9,101,298	3,592,550	3,697,810	2,304,639	1,294,718	19,991,015
Noncurrent assets:						
Restricted assets:						
Cash and pooled investments	—	—	—	—	144,203	144,203
Investments	—	—	—	—	37,473	37,473
Investments	12,470,409	15,561,973	51,707	—	836,920	28,921,009
Receivables (net)	667,879	13,500	—	—	175,700	857,079
Loans receivable	—	—	5,296,855	—	245,114	5,541,969
Deferred charges	—	39,309	31,474	—	1,605	72,388
Capital assets:						
Land	489,685	25,680	—	—	82,932	598,297
Collections – nondepreciable	245,578	—	—	—	4,867	250,445
Buildings and other depreciable property	21,736,142	385,649	1,541	—	1,406,900	23,530,232
Less: accumulated depreciation	(10,252,600)	(169,740)	(635)	—	(520,513)	(10,943,488)
Construction in progress	3,311,500	—	—	—	47,932	3,359,432
Other noncurrent assets	240,700	—	15,428	—	84,734	340,862
Total noncurrent assets	28,909,293	15,856,371	5,396,370	—	2,547,867	52,709,901
Total assets	\$ 38,010,591	\$ 19,448,921	\$ 9,094,180	\$ 2,304,639	\$ 3,842,585	\$ 72,700,916

	University of California	State Compensation Insurance	California Housing Finance Agency	Public Employees' Benefits	Nonmajor Component Units	Total
LIABILITIES						
Current liabilities:						
Accounts payable	\$ 1,496,607	\$ 172,605	\$ 45,885	\$ 6,368	\$ 99,420	\$ 1,820,885
Due to other governments	—	—	682	238,392	3,682	242,756
Deposits	297,691	—	152,100	—	1,162	450,953
Dividends payable	—	3,100	—	—	—	3,100
Deferred revenue	612,923	—	—	—	57,356	670,279
Contracts and notes payable	—	—	—	—	12,818	12,818
Advance collections	—	312,065	—	—	779	312,844
Interest payable	—	—	114,835	—	1,161	115,996
Benefits payable	—	3,029,110	—	—	—	3,029,110
Securities lending obligations	2,865,445	927,218	—	—	—	3,792,663
Current portion of long-term obligations	1,164,636	—	1,098,577	220,478	73,642	2,557,333
Other current liabilities	1,251,551	161,709	735	113,313	171,359	1,698,667
Total current liabilities	7,688,853	4,605,807	1,412,814	578,551	421,379	14,707,404
Noncurrent liabilities:						
Benefits payable	—	11,450,780	—	2,244,712	—	13,695,492
Compensated absences payable	185,965	52,814	—	—	10,342	249,121
Loans payable	—	—	—	—	9,078	9,078
Certificates of participation, commercial paper, and other borrowings	222,111	—	—	—	11,009	233,120
Capital lease obligations	1,779,604	—	—	—	155,296	1,934,900
Revenue bonds payable	4,943,557	—	6,404,308	—	495,076	11,842,941
Other noncurrent liabilities	962,942	234,512	87,658	—	332,107	1,617,219
Total noncurrent liabilities	8,094,179	11,738,106	6,491,966	2,244,712	1,012,908	29,581,871
Total liabilities	15,783,032	16,343,913	7,904,780	2,823,263	1,434,287	44,289,275
NET ASSETS						
Investment in capital assets, net of related debt	8,108,355	241,589	906	—	383,575	8,734,425
Restricted:						
Nonexpendable	2,183,735	—	—	—	540,474	2,724,209
Expendable:						
Endowments and gifts	5,720,300	—	—	—	5,928	5,726,228
Education	707,831	—	—	—	540,531	1,248,362
Indenture	—	—	721,750	—	—	721,750
Employee benefits	—	—	—	295,961	—	295,961
Workers' compensation liability	—	2,863,419	—	—	—	2,863,419
Statute	—	—	466,744	—	—	466,744
Other purposes	—	—	—	—	308,149	308,149
Total expendable	6,428,131	2,863,419	1,188,494	295,961	854,608	11,630,613
Unrestricted	5,507,338	—	—	(814,585)	629,641	5,322,394
Total net assets	22,227,559	3,105,008	1,189,400	(518,624)	2,408,298	28,411,641
Total liabilities and net assets	\$ 38,010,591	\$ 19,448,921	\$ 9,094,180	\$ 2,304,639	\$ 3,842,585	\$ 72,700,916

Statement of Revenues, Expenses, and Changes in Fund Net Assets

Discretely Presented Component Units – Enterprise Activity

Year Ended June 30, 2005

(amounts in thousands)

	University of California	State Compensation Insurance Fund	California Housing Finance Agency	Public Employees' Benefits	Nonmajor Component Units	Total
OPERATING REVENUES						
Student tuition and fees	\$ 1,557,828	\$ —	\$ —	\$ —	\$ 116,230	\$ 1,674,058
Grants and contracts	3,976,549	—	48,835	—	466,927	4,492,311
Services and sales	5,872,193	—	7,994	2,884,225	876,140	9,640,552
Department of Energy laboratories	4,146,261	—	—	—	—	4,146,261
Earned premiums (net)	—	7,918,319	—	—	—	7,918,319
Investment and interest	—	—	300,330	—	14,373	314,703
Rent	—	—	—	—	22,067	22,067
Other	383,729	20,003	7,508	1,721	96,005	508,966
Total operating revenues	15,936,560	7,938,322	364,667	2,885,946	1,591,742	28,717,237
OPERATING EXPENSES						
Personal services	8,923,998	578,870	18,944	—	253,913	9,775,725
Scholarships and fellowships	363,161	—	—	—	23,654	386,815
Supplies	1,706,728	—	—	—	5,662	1,712,390
Services and charges	310,620	61,286	67,888	3,553,260	617,026	4,610,080
Department of Energy laboratories	4,112,077	—	—	—	—	4,112,077
Depreciation	954,878	19,253	168	—	60,246	1,034,545
Distributions to beneficiaries	—	5,979,711	—	—	—	5,979,711
Interest expense	—	—	326,345	—	5,141	331,486
Amortization of deferred charges	—	853,687	1,391	—	59	855,137
Other	2,248,781	130,744	—	—	664,034	3,043,559
Total operating expenses	18,620,243	7,623,551	414,736	3,553,260	1,629,735	31,841,525
Operating income (loss)	(2,683,683)	314,771	(50,069)	(667,314)	(37,993)	(3,124,288)
NONOPERATING REVENUES (EXPENSES)						
Primary government and federal grants	2,583,742	—	74,123	—	—	2,657,865
Donations and Grants	—	—	—	—	8,246	8,246
Grants provided	(343,388)	—	(74,123)	—	(146,500)	(564,011)
Private gifts	869,469	—	—	—	131,356	1,000,825
Investment and interest income	837,687	514,026	120,169	137,383	94,868	1,704,133
Interest expense and fiscal charges ..	(295,439)	—	—	—	(27,660)	(323,099)
Other	147,117	3,932	—	—	(78,430)	72,619
Total nonoperating revenues	3,799,188	517,958	120,169	137,383	(18,120)	4,556,578
Income (loss) before contributions ..	1,115,505	832,729	70,100	(529,931)	(56,113)	1,432,290
Capital contributions	217,218	—	—	—	15,324	232,542
Permanent endowments	170,090	—	—	—	44,170	214,260
Change in net assets	1,502,813	832,729	70,100	(529,931)	3,381	1,879,092
Total net assets, July 1, 2004	20,724,746 *	2,272,279	1,119,300	11,307	2,404,917 *	26,532,549
Total net assets, June 30, 2005	\$ 22,227,559	\$ 3,105,008	\$ 1,189,400	\$ (518,624)	\$ 2,408,298	\$ 28,411,641

* Restated

Notes to the Financial Statements – Index

Note 1.	Summary of Significant Accounting Policies	35
	A. Reporting Entity	35
	1. Blended Component Units	35
	2. Fiduciary Component Units	36
	3. Discretely Presented Component Units	37
	4. Joint Venture	39
	5. Related Organizations	39
	B. Government-wide and Fund Financial Statements	40
	C. Measurement Focus and Basis of Accounting	
	1. Government-wide Financial Statements	42
	2. Fund Financial Statements	43
	D. Inventories	43
	E. Deposits and Investments	44
	F. Net Investment in Direct Financing Leases	44
	G. Deferred Charges	44
	H. Capital Assets	44
	I. Long-term Obligations	45
	J. Compensated Absences	46
	K. Net Assets and Fund Balance	46
	L. Restatement of Beginning Fund Balances and Net Assets	
	1. Fund Financial Statements	47
	2. Government-wide Financial Statements.....	47
	M. Guaranty Deposits	47
Note 2.	Budgetary and Legal Compliance	
	A. Budgeting and Budgetary Control	47
	B. Legal Compliance	48
Note 3.	Deposits and Investments	48
	A. State Treasurer's Pooled Investment Program	48
	B. Other Primary Government	51
	1. Interest Rate Risk	52
	2. Concentration of Credit Risk	55

3. Custodial Credit Risk	55
C. Fiduciary Funds	56
1. Interest Rate Risk	58
2. Concentration of Credit Risk	63
3. Foreign Currency Risk	63
D. Discretely Presented Component Units	64
1. Interest Rate Risk	66
2. Concentration of Credit Risk	69
3. Custodial Credit Risk	70
4. Foreign Currency Risk	71
Note 4. Accounts Receivable	72
Note 5. Restricted Assets	73
Note 6. Net Investment in Direct Financing Leases	74
Note 7. Capital Assets	75
Note 8. Accounts Payable	77
Note 9. Short-term Financing	78
Note 10. Long-term Obligations	78
Note 11. Certificates of Participation	79
Note 12. Commercial Paper and Other Long-Term Borrowings	80
Note 13. Leases	81
Note 14. Commitments	83
Note 15. General Obligation Bonds	84
A. Variable-Rate General Obligation Bonds	84
B. Economic Recovery Bonds	85
C. Debt Service Requirements	86
D. General Obligation Bond Defeasances	
1. Current Year	86
2. Prior Years	87
Note 16. Revenue Bonds	
A. Governmental Activities	87
B. Business-type Activities	88
C. Discretely Presented Component Units	88
D. Primary Government Variable Rate/Swap Disclosure	91
E. Discretely Presented Component Unit Variable Rate/Swap Disclosure – University of California.....	93

F. Discretely Presented Component Unit Variable Rate/Swap Disclosure – California Housing Finance Agency	93
G. Revenue Bond Defeasances	
1. Current Year	94
2. Prior Years	95
Note 17. Interfund Balances and Transfers	
A. Interfund Balances	96
B. Interfund Transfers	100
Note 18. Fund Deficits and Endowments	
A. Fund Deficits	102
B. Discretely Presented Component Unit Endowments	102
Note 19. Risk Management	102
Note 20. Nonmajor Enterprise Segment Information	104
Note 21. No Commitment Debt	108
Note 22. Contingent Liabilities	
A. Litigation	108
B. Federal Audit Exceptions	110
Note 23. Pension Trusts	110
A. Public Employees' Retirement Fund	
1. Fund Information	111
2. Employer's Information	111
B. Judges' Retirement Fund	112
C. Judges' Retirement Fund II	113
D. Legislators' Retirement Fund	113
E. Volunteer Firefighters' Length of Service Award Fund	114
F. State Peace Officers' and Firefighters' Defined Contribution Plan Fund	114
G. State Teachers' Retirement Fund	115
H. CalSTRS Voluntary Investment Program	116
I. Teachers' Health Benefits Fund	116
J. University of California Retirement System	116
Note 24. Post-Retirement Health Care Benefits	122
Note 25. Subsequent Events	122

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Notes to the Financial Statements

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements present information on the financial activities of the State of California over which the Governor, the Legislature, and other elected officials have direct or indirect governing and fiscal control. These financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP). The provisions of the following Governmental Accounting Standards Board (GASB) Statement have been implemented for the year ended June 30, 2005:

GASB Statement No. 40, *Deposit and Investment Risk Disclosures, an Amendment of GASB Statement No. 3.*

This new GASB Statement significantly changed the disclosure of risks related to the State's investments as shown in Note 3, Deposits and Investments.

A. Reporting Entity

These financial statements present the primary government of the State and its component units. The **primary government** consists of all funds, organizations, institutions, agencies, departments, and offices that are not legally separate from the State. **Component units** are organizations that are legally separate from the State but for which the State is financially accountable, or for which the nature and significance of their relationship with the State is such that exclusion would cause the State's financial statements to be misleading or incomplete. The decision to include a potential component unit in the State's reporting entity is based on several criteria, including legal standing, fiscal dependency, and financial accountability. Following is information on the blended, fiduciary, and discretely presented component units of the State.

1. Blended Component Units

Blended components units, although legally separate entities, are in substance part of the primary government's operations. Therefore, data from these blended component units are integrated into the appropriate funds for reporting purposes.

Building authorities are blended component units because they have been created through the use of joint exercise of powers agreements with various cities to finance the construction of state buildings. The building authorities are reported as capital projects funds. As a result, the \$683 million of capital lease arrangements between the building authorities and the State has been eliminated from the financial statements. Instead, only the underlying capital assets and the debt used to acquire them are reported in the government-wide financial statements. For information on how to obtain copies of the financial statements of the building authorities, contact the State Controller's Office, Division of Accounting and Reporting, P.O. Box 942850, Sacramento, California 94250.

The *Golden State Tobacco Securitization Corporation (GSTSC)* is a not-for-profit corporation established through legislation in September 2002 solely for the purpose of purchasing Tobacco Settlement Revenues from the State. The five voting members of the State Public Works Board serve ex officio as the directors of the corporation. GSTSC is authorized to issue bonds necessary to provide sufficient funds for carrying out its purpose. GSTSC is reported in the combining statements in the Nonmajor Governmental Funds section as a special revenue fund. For information on how to obtain copies of the financial statements of GSTSC, contact the Department of Finance, Capital Outlay/Resources Section, 915 L Street, 9th Floor, Sacramento, California 94250.

The *California State University, Channel Islands Site Authority (Site Authority)* was formed in 1998 to convert the property previously known as the Camarillo State Hospital from its former use to a California State University campus and other compatible uses. The Site Authority is governed by a board of seven members comprised of four representatives of the Trustees of the California State University and three representatives from Ventura County. The *California State University, Channel Islands Financing Authority (Financing Authority)* was formed in 2000 to provide financing through revenue bonds for the construction and other improvements conducted by the Site Authority. The Site Authority and the Financing Authority are included in the California State University Programs special revenue fund in the combining statements in the Nonmajor Governmental Funds section. The loan and other transactions of \$197.7 million between the two authorities have been eliminated from the financial statements. Instead, only the underlying capital assets and the debt used to acquire them are reported in the government-wide financial statements. For information on how to obtain copies of the financial statements of the Site Authority and the Financing Authority, contact the California State University, Channel Islands, One University Drive, Camarillo, California 93012.

2. Fiduciary Component Units

The State has three fiduciary component units that administer pension and other employee benefit trust funds. These entities are legally separate from the State and meet the definition of a component unit because they are fiscally dependent on the State; however, due to their fiduciary nature, they are presented in the Fiduciary Fund Statements as pension and other employee benefit trust funds, along with other primary government fiduciary funds.

The *California Public Employees' Retirement System (CalPERS)* administers pension and health benefit plans for state employees, non-teaching school employees, and employees of California public agencies. Its Board of Administration has plenary authority and fiduciary responsibility for the investment of monies and the administration of the plans. CalPERS administers the following seven pension and other employee benefit trust funds: the Public Employee's Retirement Fund, the Judges' Retirement Fund, the Judges Retirement Fund II, the Legislators' Retirement Fund, the Volunteer Firefighters' Length of Service Award Fund, the State Peace Officers' and Firefighters' Defined Contribution Plan Fund, and the Supplemental Contributions Program Fund. Copies of CalPERS' separately issued financial statements may be obtained in writing from the California Public Employees' Retirement System, Fiscal Services Division, P.O. Box 942703, Sacramento, California 94229.

The *California State Teachers' Retirement System (CalSTRS)* administers pension benefit plans for California public school teachers and certain other employees of the public school system. CalSTRS administers two pension and other employee benefit trust funds: the State Teachers' Retirement Fund and the Teachers' Health Benefits Fund. Copies of CalSTRS' separately issued financial statements may be obtained from the California State Teachers' Retirement System, P.O. Box 15275, Sacramento, California 95851.

The *University of California Retirement System (UCRS)* is part of the comprehensive benefits package that offers defined benefit plans and defined contribution plans to employees of the university. The UCRS is a fiduciary activity of the University of California, a discretely presented component unit. Copies of the University of California's separately issued financial statements may be obtained from the University of California, Financial Management, 1111 Franklin Street, 10th Floor, Oakland, California 94607.

3. Discretely Presented Component Units

Enterprise activity of discretely presented component units is reported in a separate column in the government-wide financial statements. Discretely presented component units are legally separate from the primary government and mostly provide services to entities and individuals outside the primary government. Discretely presented component units that report enterprise activity include the University of California, the State Compensation Insurance Fund, the California Housing Finance Agency, and nonmajor component units.

The *University of California* was founded in 1868 as a public, state-supported, land grant institution. It was written into the State Constitution of 1879 as a public trust to be administered by a governing board, the Regents of the University of California. The University of California is a component unit of the State because the State appoints a voting majority of the regents and because expenditures for the support of various university programs and capital outlay are appropriated by the annual Budget Act. Copies of the University of California's separately issued financial statements may be obtained from the University of California, Financial Management, 1111 Franklin Street, 10th Floor, Oakland, California 94607.

The *State Compensation Insurance Fund (SCIF)* is a self-supporting enterprise created to offer insurance protection to employers at the lowest possible cost. It operates in competition with other insurance carriers to provide services to the State, counties, cities, school districts, and other public corporations. It is a component unit of the State because the State appoints all five voting members of SCIF's governing board and has the authority to approve or modify SCIF's budget. Copies of SCIF's financial statements for the year ended December 31, 2004, may be obtained from the State Compensation Insurance Fund, 1275 Market Street, San Francisco, California 94103.

The *California Housing Finance Agency (CalHFA)* was created by the Zenovich-Moscone-Chacon Housing and Home Finance Act, as amended. CalHFA's purpose is to meet the housing needs of persons and families of low and moderate income. It is a component unit of the State because the State appoints a voting majority of CalHFA's governing board and has the authority to approve or modify its budget. Copies of CalHFA's financial statements may be obtained from the California Housing Finance Agency, P.O. Box 4034, Sacramento, California 95812.

The *Public Employees' Benefits Fund*, which is administered by the California Public Employees' Retirement System and accounts for contributions and premiums for public employee long-term care plans and for administration of a deferred compensation program. Copies of CalPERS' separately issued financial statements may be obtained in writing from the California Public Employees' Retirement System, Fiscal Services Division, P.O. Box 942703, Sacramento, California 94229.

State legislation created various *nonmajor component units* to provide certain services outside the primary government and to provide certain private and public entities with a low-cost source of financing for programs deemed to be in the public interest. The California Pollution Control Financing Authority, the San Joaquin River Conservancy, and the district agricultural associations are considered component units since they have a fiscal dependency on the primary government. The California Educational Facilities Authority is considered a component unit because its exclusion from the statements would be misleading because of its relationship with the primary government. California State University auxiliary organizations are considered component units because they exist entirely or almost entirely for the direct benefit of the universities. The remaining nonmajor component units are considered component units because the majority of members of their governing boards are appointed by or are members of the primary government, the primary government can impose its will on the entity, or the entity provides a specific financial benefit to the primary government. For information on how to obtain copies of the financial statements of these component units, contact the State Controller's Office, Division of Accounting and Reporting, P.O. Box 942850, Sacramento, California 94250.

The nonmajor component units are:

The *California Alternative Energy and Advanced Transportation Financing Authority*, which provides financing for alternative energy and advanced transportation technologies;

The *California Infrastructure and Economic Development Bank*, which provides financing for business development and public improvements;

The *California Pollution Control Financing Authority*, which provides financing for pollution control facilities;

The *California Health Facilities Financing Authority*, which provides financing for the construction, equipping, and acquisition of health facilities;

The *California Educational Facilities Authority*, which issues revenue bonds to finance loans for students attending public and private colleges and universities and to assist private educational institutions of higher learning in financing the expansion and construction of educational facilities;

The *California School Finance Authority*, which provides loans to school and community college districts to assist them in obtaining equipment and facilities;

California State University auxiliary organizations, which provide services primarily to university students through foundations, associated student organizations, student unions, food service entities, book stores, and similar organizations;

District agricultural associations, which exhibit all of the industries, industrial enterprises, resources, and products of the state (the district agricultural associations' financial report is as of and for the year ended December 31, 2004);

The *University of California Hastings College of the Law*, which was established as the law department of the University of California to provide legal education programs and operates independently under its own Board of Directors. The College has a discretely presented component unit, the Foundation, that provides private sources of funds for academic programs, scholarships, and faculty research;

The *San Joaquin River Conservancy*, which was created to acquire and manage public lands within the San Joaquin River Parkway;

The *California Urban Waterfront Area Restoration Financing Authority*, which provides financing for coastal and inland urban waterfront restoration projects; and

The *California Consumer Power and Conservation Financing Authority*, which provides financing for projects to increase power supplies, reduce demand for energy, and improve the efficiency and environmental performance of power plants.

4. Joint Venture

A joint venture is an entity resulting from a contractual arrangement and owned, operated, or governed by two or more participants as a separate and specific activity subject to joint control. In such an arrangement, the participants retain an ongoing financial interest or an ongoing financial responsibility in the entity. These entities are not part of the primary government or a component unit.

The State participates in a joint venture with the *Capitol Area Development Authority (CADA)*. CADA was created in 1978 by the joint exercise of powers agreement between the primary government and the City of Sacramento for the location of state buildings and other improvements. CADA is a public entity, separate from the primary government and the city, and is administered by a board of five members: two appointed by the primary government, two appointed by the city, and one appointed by the affirmative vote of at least three of the other four members of the board. The primary government designates the chairperson of the board. Although the primary government does not have an equity interest in CADA, it does have an ongoing financial interest. Based upon the appointment authority, the primary government has the ability to indirectly influence CADA to undertake special projects for the citizenry of the participants. The primary government subsidizes CADA's operations by leasing land to CADA without consideration; however, the primary government is not obligated to do so. At June 30, 2005, CADA had total assets of \$26.0 million, total liabilities of \$18.0 million, and total net assets of \$8.0 million. Total revenues for the fiscal year were \$8.5 million and expenses were \$7.7 million, resulting in a net income of \$753,792. Because the primary government does not have an equity interest in CADA, CADA's financial information is not included in the financial statements of this report. Separately issued financial statements may be obtained from the Capitol Area Development Authority, 1522 14th Street, Sacramento, California 95814.

5. Related Organizations

A related organization is an organization for which a primary government is accountable because that government appoints a voting majority of the organization's governing board, but which is not financially accountable to the State.

Chapter 854 of the Statutes of 1996 created an *Independent System Operator*, a state-chartered, nonprofit market institution. The Independent System Operator is responsible for providing centralized control of the statewide transmission grid to ensure the efficient use and reliable operation of the transmission system. A five-member oversight board, comprised of three Governor appointees, an appointee of the Senate Committee on Rules, and an appointee of the Speaker of the Assembly, oversees the Independent System Operator and appoints a governing board that is broadly representative of the state's electricity users and providers. The State's accountability for this institution does not extend beyond making the appointments. Because the primary government is not financially accountable for the Independent System Operator, the financial information of this institution is not included in the financial statements of this report. For information on how to obtain copies of the financial statements of the Independent System Operator, contact the State Controller's Office, Division of Accounting and Reporting, P.O. Box 942850, Sacramento, CA 94250.

The *California Earthquake Authority (CEA)*, a legally separate organization, offers basic earthquake insurance for California homeowners, renters, condominium owners, and mobilehome owners. A three-member board of state elected officials governs the CEA. The State's accountability for this institution does not extend beyond making the appointments. Because the primary government is not financially accountable for the CEA, the financial information of this institution is not included in the financial statements of this report. For information on how to obtain copies of the financial statements of the CEA, contact the California Earthquake Authority, 801 K Street, Suite 1000, Sacramento, CA 95814.

The *Bay Area Toll Authority*, which is not part of the State's reporting entity, was created by the California Legislature in 1997 to administer the base \$2 toll on toll revenues collected from the San Francisco Bay Area's seven state-owned toll bridges and to have program oversight related to certain bridge construction projects. Additional information on the Bay Area Toll Authority may be obtained from the Metropolitan Transportation Commission, 101 Eighth Street, Oakland, California 94607.

B. Government-wide and Fund Financial Statements

Government-wide financial statements (the Statement of Net Assets and the Statement of Activities) report information on all the nonfiduciary activities of the primary government and its component units. The primary government is reported separately from legally separate component units for which the State is financially accountable. Within the primary government, the State's governmental activities, which are normally supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. The effect of interfund activity has been removed from the statements, with the exception of amounts between governmental and business-type activities, which are presented as internal balances and transfers. Centralized services provided by the General Fund for other funds are charged as direct costs to the funds that received those services. Also, the General Fund recovers from the federal government the cost of centralized services provided to federal programs.

The Statement of Net Assets reports all of the financial and capital resources of the government as a whole in a format where assets equal liabilities plus net assets. The statement of activities demonstrates the degree to which the expenses of a given function are offset by program revenues. Program revenues include charges to customers who purchase, use, or directly benefit from goods, services, or privileges provided by a given function. Program revenues also include grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. Taxes and other items that are not program-related are reported as general revenues.

Fund financial statements are provided for governmental funds, proprietary funds, fiduciary funds and similar component units, and discretely presented component units. A fund is a fiscal and accounting entity with a self-balancing set of accounts. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with finance-related legal and contractual provisions. The minimum number of funds is maintained that is consistent with legal and managerial requirements. Fiduciary funds, although excluded from the government-wide statements, are included in the fund financial statements. Major governmental and enterprise funds are reported in separate columns in the fund financial statements. Nonmajor governmental and proprietary funds are grouped into separate columns. Discretely presented component unit statements, which follow the fiduciary fund statements, also separately report the enterprise activity of the major discretely presented component units. The enterprise activity of nonmajor discretely presented component units is grouped in a separate column.

Governmental fund types are used primarily to account for services provided to the general public without charging directly for those services.

The State reports the following major governmental funds.

The *General Fund* is the main operating fund of the State. It accounts for transactions related to resources obtained and used for those services that do not need to be accounted for in another fund.

The *Federal Fund* accounts for the receipt and use of grants, entitlements, and shared revenues received from the federal government.

The *Transportation Construction Fund* accounts for gasoline taxes, bond proceeds, and other revenues that are used for highway and passenger rail construction.

Proprietary fund types focus on the determination of operating income, changes in net assets, financial position, and cash flows.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

For its proprietary funds, the State applies all applicable GASB pronouncements. In addition, the State applies all applicable Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board (APB) Opinions, and Committee on Accounting Procedure (CAP) Accounting Research Bulletins issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements. The State has elected not to apply FASB pronouncements issued after November 30, 1989, for its enterprise funds.

The State has two proprietary fund types: enterprise funds and internal service funds.

Enterprise funds record business-type activity for which a fee is charged to external users for goods and services. In addition, the State is required to report activities as enterprise funds in the context of the activity's principal revenue sources when any of the following criteria are met:

1. The activity's debt is secured solely by fees and charges of the activity;
2. There is a legal requirement to recover costs; or
3. The pricing policies of fees and charges are designed to recover costs.

The State reports the following *major enterprise funds*.

The *Electric Power Fund* accounts for the acquisition and resale of electric power to retail end-use customers.

The *Water Resources Fund* accounts for charges to local water districts and the sale of excess power to public utilities.

The *Public Building Construction Fund* accounts for rental charges from the lease of public assets.

The *State Lottery Fund* accounts for the sale of California State Lottery (Lottery) tickets and the Lottery's payments for education.

The *Unemployment Programs Fund* accounts for employer and worker contributions used for payments of unemployment insurance and disability benefits.

Nonmajor enterprise funds account for additional operations that are financed and operated in a manner similar to private business enterprises.

Additionally, the State reports *internal service funds* as a proprietary fund type with governmental activity. Internal service funds account for goods or services provided to other agencies, departments, or governments on a cost-reimbursement basis. The goods and services provided include: architectural services, construction and improvements, printing and procurement services, goods produced by inmates of state prisons, data processing services, administrative services related to water delivery, and equipment used by the California Department of Transportation. Internal service funds are included in the governmental activities at the government-wide level.

Fiduciary fund types are used to account for assets held by the State. The State acts as a trustee or as an agent for individuals, private organizations, other governments, or other funds. Fiduciary funds, including fiduciary component units, are not included in the government-wide financial statements.

The State has the following four fiduciary fund types.

Private purpose trust funds account for all trust arrangements, other than those properly reported in pension or investment trust funds, whereby principal and income benefit individuals, private organizations, or other governments.

Pension and other employee benefit trust funds of the primary government and fiduciary component units account for transactions, assets, liabilities, and net assets available for plan benefits of the retirement systems and for other employee benefit programs.

An *investment trust fund* accounts for the deposits, withdrawals, and earnings of the Local Agency Investment Fund, an external investment pool for local governments and public agencies.

Agency funds account for assets held by the State, which acts as an agent for individuals, private organizations, or other governments.

Discretely presented component units consist of certain organizations that have enterprise activity. The enterprise activity component units are the University of California, the State Compensation Insurance Fund, the California Housing Finance Agency, Public Employees' Benefits Fund, and nonmajor component units. All of the enterprise activity of the discretely presented component units is reported in a separate column in the government-wide financial statements and on separate pages following the fund financial statements.

C. Measurement Focus and Basis of Accounting

1. Government-wide Financial Statements

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a

liability is incurred, regardless of the timing of related cash flows. Grants and similar transactions are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

2. Fund Financial Statements

The measurement focus and basis of accounting for the fund financial statements vary with the type of fund. **Governmental fund types** are presented using the current financial resources measurement focus. With this measurement focus, operating statements present increases and decreases in net current assets; the unreserved fund balance is a measure of available spendable resources.

The accounts of the governmental fund types are reported using the modified accrual basis of accounting. Under the modified accrual basis, revenues are recorded as they become measurable and available, and expenditures are recorded at the time the liabilities are incurred. Principal tax revenues susceptible to accrual are recorded as taxpayers earn income (personal income and corporation taxes), as sales are made (consumption and use taxes), and as the taxable event occurs (miscellaneous taxes), net of estimated tax overpayments. Other revenue sources are recorded when they are earned or when they are due, provided they are measurable and available within the ensuing 12 months.

Agency funds are custodial in nature and do not measure the results of operations. Assets and liabilities are recorded using the modified accrual basis of accounting.

Proprietary fund types, the **investment trust fund**, **private purpose trust funds**, and **pension and other employee benefit trust funds** are accounted for using the economic resources measurement focus.

The accounts of the proprietary fund types, the investment trust fund, private purpose trust funds, and pension and other employee benefit trust funds are reported using the accrual basis of accounting. Under the accrual basis, most transactions are recorded when they occur, regardless of when cash is received or disbursed.

Lottery revenue and the related prize expenses are recognized when sales are made. Certain prizes are payable in deferred installments. Such liabilities are recorded at the present value of amounts payable in the future.

For purposes of the Statement of Cash Flows, all cash and pooled investments in the State Treasurer's pooled investment program are considered to be cash and cash equivalents.

Discretely presented component units are accounted for using the economic resources measurement focus and the accrual basis of accounting.

D. Inventories

Inventories of supplies are reported at cost and inventories held for resale are stated at the lower of average cost or market. In the government-wide financial statements, inventories for both governmental and business-type activities are expensed when consumed and unused inventories are reported as an asset on the Statement of Net Assets. In the fund financial statements, governmental funds report inventories as expenditures when purchased, and proprietary funds report inventories as expenditure when consumed.

The discretely presented component units have inventory policies similar to those of the primary government.

E. Deposits and Investments

The State reports investments at fair value, as prescribed by GAAP. Additional information on the State's investments can be found in Note 3, Deposits and Investments.

F. Net Investment in Direct Financing Leases

The State Public Works Board, an agency that accounts for its activities as an enterprise fund, has entered into lease-purchase agreements with various other primary government agencies, the University of California, and certain local agencies. The payments from these leases are used to satisfy the principal and interest requirements of revenue bonds issued by the State Public Works Board to finance the cost of projects such as acquisition and construction of facilities and equipment. Upon expiration of these leases, jurisdiction of the facilities and projects transfers to the primary government agency, the University of California, or the local agency. The State Public Works Board records the net investment in direct financing leases at the net present value of the minimum lease payments.

G. Deferred Charges

The deferred charges account primarily represents operating and maintenance costs and unrecovered capital costs in the enterprise fund type that will be recognized as expenses over the remaining life of long-term state water supply contracts in the Water Resources Fund. These costs are billable in future years. In addition, the account includes unbilled interest earnings on unrecovered capital costs that are recorded as deferred charges. These charges are recognized when billed in future years under the terms of water supply contracts. The deferred charges for the Public Buildings Construction Fund include bond counsel fees, trustee fees, rating agency fees, underwriting costs, insurance costs, and miscellaneous expenses. Bond issuance costs are amortized using the straight-line method over the term of the bonds. Amortization of bond issue costs during the facility construction period is capitalized and included in the construction costs. Deferred charges are also included in the State Lottery Fund and nonmajor enterprise funds. Bond discounts and issuance costs recorded as expenditures in certain capital projects and special revenue funds are reclassified as deferred charges in the governmental activities column of the Statement of Net Assets.

H. Capital Assets

Capital assets are categorized into land, state highway infrastructure, collections, buildings and other depreciable property, and construction in progress. The buildings and other depreciable property account includes buildings, improvements other than buildings, equipment, personal property, intangible assets, certain infrastructure assets, certain books, and other capitalized and depreciable property. The value of the capital assets, including the related accumulated depreciation, is reported in the applicable governmental, business-type, or component unit activities columns in the government-wide Statement of Net Assets.

The primary government has a large collection of historical and contemporary treasures that have important documentary and artistic value. These assets are not capitalized or depreciated, because they are cultural resources and cannot reasonably be valued and/or the assets have inexhaustible useful lives. These treasures and works of art consist of furnishings, portraits and other paintings, books, statues, photographs, and miscellaneous artifacts. These collections meet the conditions for exemption from capitalization because the collections are: held for public exhibition, education, or research in furtherance of public service, rather than financial gain; protected, kept unencumbered, cared for, and preserved; and are subject to an organizational policy that requires the proceeds from sales of collection items to be used to acquire other items for collections.

In general, capital assets of the primary government are defined as assets that have a normal useful life of at least one year and a unit acquisition cost of at least \$5,000. These assets are recorded at historical cost or estimated historical cost, including all costs related to the acquisition. Donated capital assets are recorded at the fair market value on the date the gift was received. Major capital asset outlays are capitalized as projects are constructed.

Buildings and other depreciable property are depreciated using the straight-line method with no salvage value for governmental activities. Buildings and other improvements are depreciated over 40 years. Equipment and personal property are depreciated over 5 years. Buildings and other depreciable property used by the California State University are depreciated from 3 to 45 years. Depreciable assets of business-type activities are depreciated using the straight-line method over their estimated useful or service lives, ranging from 2 to 100 years.

California has elected to use the modified approach for capitalizing the infrastructure assets of the state highway system. The state highway system consists of over 49,000 lane-miles and over 12,000 bridges that are maintained by the California Department of Transportation. By using the modified approach, the infrastructure assets of the state highway system are not depreciated and all expenditures made for those assets, except for additions and improvements, are expensed in the period incurred. All additions and improvements made after June 30, 2001, are capitalized. All infrastructure assets that are related to projects completed prior to July 1, 2001, are recorded at the historical costs contained in annual reports of the American Association of State Highway and Transportation Officials (AASHTO) and the Federal Highway Administration.

The capital assets of the discretely presented component units are reported at cost at the date of acquisition, or at fair market value at the date of donation in the case of gifts. They are depreciated over their estimated useful service lives.

I. Long-term Obligations

Long-term obligations consist of certain unmatured general obligation bonds, certain unmatured revenue bonds, capital lease obligations, certificates of participation, commercial paper, the net pension obligation of the pension and other employee benefit trust funds, the liability for employees' compensated absences and workers' compensation claims, amounts owed for lawsuits, reimbursement for costs mandated by the State, the outstanding Proposition 98 funding guarantee owed to schools, the liability for Lottery prizes and annuities, and the primary government's share of the University of California pension liability that is due in more than one year. In the government-wide financial statements, current and noncurrent obligations are reported as liabilities in the applicable governmental activities, business-type activities, and component units columns of the Statement of Net Assets.

Bond premiums and discounts, as well as issuance costs, for business-type activities and component units are generally deferred and amortized over the life of the bonds. In these instances, bonds payable are reported net of the applicable premium or discount and bond issuance costs are reported as deferred charges. Bond premiums and discounts, as well as issuance costs, for governmental activities are expensed in the year incurred in the fund financial statements. These costs are reported as deferred charges in the government-wide financial statements.

With approval in advance from the Legislature, certain authorities and state agencies may issue revenue bonds. Principal and interest on revenue bonds are payable from the pledged revenues of the respective funds, building authorities, and agencies. The General Fund has no legal liability for payment of principal and

interest on revenue bonds. With the exception of certain special revenue funds (Transportation Construction, California State University Programs, and the Golden State Tobacco Securitization Corporation) and the building authorities' capital projects funds, the liability for revenue bonds is recorded in the respective fund.

J. Compensated Absences

The government-wide financial statements report both the current and the noncurrent liabilities for compensated absences, which are vested unpaid vacation and annual leave. However, unused sick-leave balances are not included in the compensated absences because they do not vest to employees. In the fund financial statements for governmental funds, no liabilities are accrued, because it is anticipated that compensated absences will not be used in excess of a normal year's accumulation. The amounts of vested unpaid vacation and annual leave accumulated by state employees are accrued in proprietary funds when incurred. In the discretely presented component units, the compensated absences are accounted for as in the proprietary funds of the primary government.

K. Net Assets and Fund Balance

The difference between fund assets and liabilities is called "net assets" on the government-wide financial statements, the proprietary and fiduciary fund statements, and the component unit statements; it is called "fund balance" on the governmental fund statements. The government-wide financial statements have the following categories of net assets.

Investment in capital assets, net of related debt, represents capital assets, net of accumulated depreciation, reduced by the outstanding principal balances of debt attributable to the acquisition, construction, or improvement of those assets.

Restricted net assets result from transactions with purpose restrictions and are designated as either *nonexpendable* or *expendable*. *Nonexpendable restricted net assets* are subject to externally imposed restrictions that must be retained in perpetuity. *Expendable restricted net assets* are subject to externally imposed restrictions that can be fulfilled by actions of the State.

Unrestricted net assets are neither restricted nor invested in capital assets, net of related debt.

In the fund financial statements, proprietary funds have similar categories of net assets. Governmental funds have two sections: *reserved and unreserved*. Part or all of the total fund balance may be reserved as a result of law or generally accepted accounting principles. Reserves represent those portions of the fund balances that are segregated for specific uses. The reserves of the fund balance for governmental funds are as follows.

Reserved for encumbrances represents goods and services that are ordered, but not received, by the end of the fiscal year.

Reserved for interfund receivables represents advances to other funds that do not represent expendable available financial resources.

Reserved for loans receivable represents the noncurrent portion of loans receivable that does not represent expendable available financial resources.

Reserved for continuing appropriations represents the unencumbered balance of all appropriations for which the period of availability extends beyond the period covered in the report. These appropriations are legally segregated for a specific future use.

The *unreserved* amounts represent the net of total fund balance, less reserves for governmental funds.

Fiduciary fund net assets are “amounts held in trust for benefits and other purposes.”

L. Restatement of Beginning Fund Balances and Net Assets

1. Fund Financial Statements

The beginning fund balance of the **nonmajor governmental funds** was increased by a total of \$97 million as a result of prior-period adjustments to correct errors, including the omission of \$85 million in loans receivable.

Beginning net assets of the **discretely presented component units – enterprise activity** were increased by a total of \$140 million. Of the total increase, \$91 million was the result of reporting University of California Hastings School of the Law as an additional nonmajor discretely presented component unit. The remaining increase is composed of a \$35 million change in accounting principle for the University of California and a net \$14 million prior period adjustment to correct errors for two other nonmajor component units.

2. Government-wide Financial Statements

The beginning net assets of the **governmental activities** and the **component units** were restated as described in the previous section for nonmajor governmental funds and discretely presented component units – enterprise activity, respectively.

M. Guaranty Deposits

The State is custodian of guaranty deposits held to protect consumers, to secure the State’s deposits in financial institutions, and to ensure payment of taxes and fulfillment of obligations to the State. Guaranty deposits of securities and other properties are not shown on the financial statements.

NOTE 2: BUDGETARY AND LEGAL COMPLIANCE

A. Budgeting and Budgetary Control

The State’s annual budget is prepared primarily on a modified accrual basis for governmental funds. The Governor recommends a budget for approval by the Legislature each year. This recommended budget includes estimated revenues; however, revenues are not included in the annual budget bill adopted by the Legislature. Under state law, the State cannot adopt a spending plan that exceeds estimated revenues.

Under the State Constitution, money may be drawn from the treasury only through a legal appropriation. The appropriations contained in the Budget Act, as approved by the Legislature and signed by the Governor, are the primary sources of annual expenditure authorizations and establish the legal level of control at the appropriation level for the annual operating budget. The budget can be amended throughout the year by special legislative action, budget revisions by the Department of Finance, or executive orders of the Governor.

Amendments to the original budget for the year ended June 30, 2005, were legally made, and they had the effect of increasing spending authority for the year.

Appropriations are generally available for expenditure or encumbrance either in the year appropriated or for a period of three years if the legislation does not specify a period of availability. At the end of the availability period, the encumbering authority for the unencumbered balance lapses. Some appropriations continue indefinitely, while others are available until fully spent. Generally, encumbrances must be liquidated within two years from the end of the period when the appropriation is available. If the encumbrances are not liquidated within this additional two-year period, the spending authority for these encumbrances lapses.

B. Legal Compliance

State agencies are responsible for exercising basic budgetary control and ensuring that appropriations are not overspent. The State Controller's Office is responsible for overall appropriation control and does not allow expenditures in excess of authorized appropriations.

Financial activities are mainly controlled at the appropriation level but can vary, depending on the presentation and wording contained in the Budget Act. Certain items that are established at the category, program, component, or element level can be adjusted by the Department of Finance. For example, an appropriation for support may have detail accounts for personnel services, operating expenses and equipment, and reimbursements. The Department of Finance can authorize adjustments between the detail accounts but cannot increase the amount of the overall support appropriation. While the financial activities are controlled at various levels, the legal level of budgetary control, or the extent to which management may amend the budget without seeking approval of the governing body, has been established in the Budget Act at the appropriation level for the annual operating budget.

NOTE 3: DEPOSITS AND INVESTMENTS

The State reports investments at fair value. State statutes authorize investments in certain types of securities. The State Treasurer administers a single pooled investment program comprising both an internal investment pool and an external investment pool (the Local Agency Investment Fund). There is a single portfolio of investments, with all participants having an undivided interest in the portfolio. Both pools are administered in the same manner, as described below. In addition, certain funds have the authority to separately invest their cash.

A. State Treasurer's Pooled Investment Program

The State's pooled investment program and certain funds of the primary government are allowed by state statutes, bond resolutions, and investment policy resolutions to have investments in United States government securities, negotiable certificates of deposit, bankers' acceptances, commercial paper, corporate bonds, bank notes, mortgage loans and notes, other debt securities, repurchase agreements, reverse repurchase agreements, equity securities, real estate, mutual funds, and other investments.

The State Treasurer's Office administers a pooled investment program for the primary government and for certain discretely presented component units. As of June 30, 2005, the discretely presented component units' cash and pooled investments were approximately 3.6% of the State Treasurer's pooled investment portfolio. This program enables the State Treasurer's Office to combine available cash from all funds and to invest cash that exceeds current needs.

Both deposits and investments are included in the State's investment program. The State Treasurer's Office maintains cash deposits with certain banks where the income earned on the deposits compensates the banks for services and uncleared checks that are deposited in the pooled investment program's accounts.

All demand and time deposits held by financial institutions as of June 30, 2005, totaling approximately \$7.6 billion, were insured by federal depository insurance or by collateral held by the State Treasurer's Office or an agent of the State Treasurer's Office in the State's name. The California Government Code requires collateral pledged for demand and time deposits to be deposited with the State Treasurer.

As of June 30, 2005, the State Treasurer's Office had amounts on deposit with a fiscal agent totaling \$30 million related to principal and interest payments to bondholders. Additionally, there was \$11 million in a compensating balance account with a custodial agent, which was designed to provide sufficient earnings to cover fees for custodial services. Most of these deposits are insured by federal depository insurance or by collateral held by an agent of the State Treasurer's Office in the State's name.

The State Treasurer's Office reports its investments at fair value. The fair value of securities in the State Treasurer's pooled investment program generally is based on quoted market prices. As of June 30, 2005, the weighted average maturity of the securities in the pooled investment program administered by the State Treasurer's Office was approximately 165 days. Weighted average maturity is the average number of days, given a dollar-weighted value of the individual investments, that the securities in the portfolio have remaining from evaluation date (date of the specific portfolio) to stated maturity.

MBS securities were purchased with average lives of 3 years and 5 years. Original average lives were determined by assuming prepayment speeds based on the interest rate environment at the time of the investment. Current average lives assume the same prepayment speed and are based on current outstanding principal and the weighted average life remaining on this principal from evaluation date (June 30, 2005) to original average life maturity (determined on purchase date.)

The Pooled Money Investment Board provides regulatory oversight over the State Treasurer's pooled investment program. The purpose of the board is to design an effective cash management and investment program, using all monies flowing through the State Treasurer's Office bank accounts and keeping all available funds invested in a manner consistent with the goals of safety, liquidity, and yield. The Pooled Money Investment Board is comprised of the State Treasurer as chair, the State Controller, and the Director of Finance. This board designates the amounts of temporarily idle money available for investment. The State Treasurer is charged with making the actual investment transactions for this program. This investment program is not registered with the Securities and Exchange Commission as an investment company.

The value of the deposits in the State Treasurer's pooled investment program, including the Local Agency Investment Fund, is equal to the dollars deposited in the program. The fair value of the position in the program may be greater or less than the value of the deposits, with the difference representing the unrealized gain or loss. As of June 30, 2005, this difference was immaterial to the valuation of the program. The pool is run with "dollar-in, dollar-out" participation. There are no share-value adjustments to reflect changes in fair value.

Certain funds have elected to participate in the pooled investment program, even though they have the authority to make their own investments. Others may be required by legislation to participate in the program. As a result, the deposits of these funds or accounts may be considered involuntary. However, these funds or accounts are part of the State's reporting entity. The remaining participation in the pool, the Local Agency Investment Fund, is voluntary.

Certain funds that have deposits in the State Treasurer's pooled investment program do not receive the interest earnings on their deposits. Instead, the earnings are legally required to be assigned to the State's General Fund. Some of the \$233 million in interest revenue received by the General Fund from the pooled investment program in the 2004-05 fiscal year was earned on balances in these funds.

The State Treasurer's pooled investment program values participants' shares on an amortized cost basis. Specifically, the program distributes income to participants quarterly, based on their relative participation during the quarter. This participation is calculated based on (1) realized investment gains and losses calculated on an amortized cost basis, (2) interest income based on stated rates (both paid and accrued), (3) amortization of discounts and premiums on a straight-line basis, and (4) investment and administrative expenses. This method differs from the fair value method used to value investments in these financial statements, because the amortized cost method is not designed to distribute to participants all unrealized gains and losses in the fair value of the pool's investments. Because the total difference between the fair value of the investments in the pool and the value distributed to pool participants using the amortized cost method described above is not material, no adjustment was made to the financial statements.

The State Treasurer's Office also reports participant fair value as a ratio of amortized cost on a quarterly basis. The State Treasurer's Office has not provided or obtained a legally binding guarantee to support the principal invested in the investment program.

As of June 30, 2005, structured notes and asset-backed securities comprised slightly more than 2.4% of the pooled investments. A significant portion of the asset-backed securities consists of small-business loans and mortgage-backed securities. The small-business loans held in the portfolio are guaranteed by the Small Business Administration, an agency of the federal government. The mortgage-backed securities, which are called real estate mortgage investment conduits (REMICs), are securities backed by pools of mortgages. The REMICs in the State's portfolio have a fixed principal payment schedule. A portion of these securities consisted of floating-rate note securities. For floating-rate notes held in the portfolio during the fiscal year, the interest received by the State Treasurer's pooled investment program rose or fell as the underlying index rate rose or fell. The structure of the floating-rate notes in the State Treasurer's pooled investment program portfolio was such that it hedged the portfolio against the risk of increasing interest rates.

The California Government Code allows the State Treasurer's Office to enter into repurchase agreements as part of its pooled investment program. A repurchase agreement consists of two simultaneous transactions. One is the purchase of securities by the State Treasurer's Office from a bank or dealer. The other is a commitment by the bank or dealer to repurchase the securities from the State Treasurer's Office at the same price, plus interest, at a mutually agreed-upon date. As the investor, the State is protected by underlying specific government securities, which are pledged as collateral during the length of the investment. During the year ended June 30, 2005, the State Treasurer's Office entered into ten repurchase agreements, with a carrying value of approximately \$1.2 billion. As of June 30, 2005, the State Treasurer's Office did not have any repurchase agreements outstanding.

The California Government Code allows the State Treasurer's Office to enter into reverse repurchase agreements as part of its pooled investment program. A reverse repurchase agreement is a sale of securities with a simultaneous agreement to repurchase them in the future at the same price plus a contract rate of interest. The fair value of the securities underlying reverse repurchase agreements normally exceeds the cash received, providing the dealers a margin against a decline in the fair value of the securities. If the dealers defaulted on their obligations to resell these securities to the State Treasurer's Office or to provide securities or cash of equal value, the State Treasurer's pooled investment program would suffer an economic loss equal to the difference between the fair value plus the accrued interest of the underlying securities and the agreement obligation, including accrued interest. During the year ended June 30, 2005, the State Treasurer's Office

entered into eight reverse repurchase agreements by temporarily selling investments with a carrying value of approximately \$1.2 billion. The maturities of investments made with the proceeds from reverse repurchase agreements are matched to the maturities of the agreements. As of June 30, 2005, the State Treasurer's Office did not have any reverse repurchase agreements outstanding.

Enterprise funds, special revenue funds, and a building authority in the capital projects funds of the primary government also make separate investments, which are presented at fair value.

B. Other Primary Government

Table 1 identifies the investment types that are authorized by the California Government Code and the State Treasurer's Office investment policy for the pooled investment program.

Table 1

Investments Authorized by the California Government Code and the State Treasurer's Office Investment Policy*

Authorized Investment Type	Maximum Maturity	Maximum Percentage of Portfolio	Maximum Investment in One Issuer
U.S. Treasury Securities	5 years*	N/A**	N/A**
Federal Agency Securities	5 years*	N/A**	N/A**
Certificates of Deposit	5 years*	N/A**	N/A**
Bank Notes	5 years*	N/A**	N/A**
Time Deposits	5 years*	N/A**	Shall not exceed net equity of the institution
Banker's Acceptances	180 days*	N/A**	N/A**
Commercial Paper	180 days	30%	10% of issuer's outstanding Commercial Paper
Corporate Bonds/Notes	5 years*	N/A**	N/A**
Repurchase Agreements	1 year*	N/A**	N/A**
Reverse Repurchase Agreements	1 year*	10%*	N/A**
Mortgages	5 years avg. life*	N/A**	N/A**

* Pursuant to State Treasurer's Office Investment Policy for the Pooled Money Investment Account.

** N/A = The State Treasurer's Office Investment Policy for the Pooled Money Investment Account has no maximum for this investment type.

1. Interest Rate Risk

Table 2 presents the primary government's investments by interest rate risk

Table 2**Schedule of Investments – Primary Government – Interest Rate Risk**

June 30, 2005

(amounts in thousands)

	Interest Rates*	Maturity	Fair Value at Year End	Weighted Average Maturity (in years)
Pooled investments				
U.S. Treasury bills and notes	1.50 – 3.45	46 days - 1.42 years	\$ 5,680,299	0.58
U. S. Agency bonds and discount notes	1.36 – 3.95	5 days - 2.2 years	13,321,547	0.61
Small Business Administration loans	3.05 – 3.88	.25 years	718,199	0.25 **
Mortgage-backed securities #	3.92 – 14.25	1 day - 5 years	531,822	1.98
Certificates of deposit	2.80 – 3.51	1 day - .42 year	14,434,037	0.16
Commercial paper	2.87 – 3.42	1 day - .42 year	10,591,838	0.10
Corporate bonds and notes	1.44 – 6.48	1 day - 1.96 years	2,894,788	0.48 ***
Total pooled investments			48,172,530	
Other primary government investments				
U.S. Treasuries and agencies			2,736,231	6.05
Commercial paper			458,459	N/A ****
Guaranteed investment contracts			722,773	16.10
Corporate debt securities			155,718	2.09
Other			226,997	2.49
Total other primary government investments			4,300,178	
Funds outside primary government included in pooled investments				
Less: investment trust funds			18,662,977	
Less: other trust and agency funds			2,380,312	
Less: discretely presented component units			2,193,105	
Total primary government investments			\$ 29,236,314	

* These interest rates represent high and low monthly averages for each investment type during the year.

** In calculating SBA holdings weighted average maturity, State Treasurer's Office assumes stated maturity is the quarterly reset date.

For corporate bond floating rate securities, State Treasurer's Office assumes final maturity date in calculating weighted average maturity.

*** These commercial paper holdings of the Golden State Tobacco Securitization Corporation mature in less than 1 year.

These securities are issued by U. S. government agencies such as the Federal National Mortgage Association.

Table 3 identifies the debt securities that are highly sensitive to interest rate fluctuations (to a greater degree than already indicated in the information provided above).

Table 3

Schedule of Debt Securities – Primary Government – Interest Rate Risk

June 30, 2005

(amounts in thousands)

Highly Sensitive Investments	Fair Value at Year End	% of Total Pooled Investments
Pooled investments		
Asset-backed		
Federal Agency CMOs	\$ 529,282	0.88 %
GNMA Pools	356	0.00 *
FHLMC PC Pools	2,184	0.00 *

The Federal Agency CMOs, GNMA and FHLMC securities are mortgage-backed securities which entitle the purchaser to receive a share of the cash flows, such as principal and interest payments, from a pool of mortgages. Mortgage securities are sensitive to interest rate changes because principal payments either increase (in a low interest rate environment) or decrease (in a high interest rate environment). A change, up or down, of the payment speed will result in a change in the yield of the security.

* Less than one-hundredth percent

Table 4 presents the primary government's debt securities by credit risk.

Table 4**Schedule of Debt Securities – Primary Government – Credit Risk**

June 30, 2005

(amounts in thousands)

Credit Rating as of Year End		
Short-term	Long-term	Fair Value
Pooled investments*		
A-1+	AAA	\$ 33,433,909
A-1	AA	6,776,869
A-2	A	884,641
	BB**	146,791
Not rated		531,822
Not applicable		6,398,498
Total pooled investments		\$ 48,172,530
Other primary government investments		
A-1+	AAA	\$ 1,080,783
A-1	AA	273,282
A-2	A	133,512
Not rated		298,299
Not applicable		2,514,302
Total other primary government investments		\$ 4,300,178

* The Treasurer's Office utilizes S&P, Moody's and Fitch ratings services. Securities are classified by lowest rating of the three agencies. All securities were within minimum legal rating requirements when purchased.

** This holding represents multiple maturities of one issuer, General Motors Acceptance Corporation.

2. Concentration of Credit Risk

The investment policy of the State Treasurer's Office contains no limitations on the amount that can be invested in any one issuer beyond that stipulated in the California Government Codes. Table 5 identifies debt securities in any one issuer (other than U.S. Treasury securities) that represent 5% or more of the State Treasurer's investments.

Table 5

Schedule of Debt Securities – Primary Government – Concentration of Credit Risk

June 30, 2005

(amounts in thousands)

Pooled investments

Issuer	Investment Type	Reported Amount	% of Total Pooled Investments
Federal Home Loan Mortgage Corp.	Federal agency securities	\$ 7,018,732	11.61 %
Federal Home Loan Bank	Federal agency securities	5,684,851	9.40
General Electric Capital/GE Company	Corporate Bonds/Commercial Paper	3,502,883	5.79

Other primary government investments

Issuer	Investment Type	Reported Amount	% of Total Agency Investments
Golden State Tobacco Securitization Corporation			
American General Finance	Commercial paper	\$ 63,450	13.84 %
Briarwood	Commercial paper	63,543	13.86
Morgan Stanley	Commercial paper	134,925	29.43
SBLI	Commercial paper	65,010	14.18
Golden Fish LLC	Commercial paper	71,061	15.50
Landesbank Baden Wurttemberg	Commercial paper	60,470	13.19
California State University			
Federal Home Loan Bank	Federal agency securities	\$ 91,905	6.30 %
Department of Veterans Affairs			
Bayerische Landesbank	Guaranteed investment contracts	\$ 62,193	41.87 %
Societe Generale	Guaranteed investment contracts	16,440	11.07
Westdeutsche Landesbank	Guaranteed investment contracts	62,182	41.86

3. Custodial Credit Risk

The State of California has a deposit policy for custodial credit risk. As of June 30, 2005, \$10 million in deposits were held in uninsured and uncollateralized accounts with U.S. Bank.

C. Fiduciary Funds

The fiduciary funds include pension and other employee benefit trust funds of the following fiduciary component units: the California Public Employees' Retirement System (CalPERS), the California State Teachers' Retirement System (CalSTRS), and the University of California Retirement System (UCRS).

CalPERS and CalSTRS exercise their authority under the State Constitution to invest in stocks, bonds, mortgages, real estate, and other investments.

The fair value of CalPERS' investments in securities is generally based on published market prices and quotations from major investment firms. Many factors are considered in arriving at fair value. In general, however, corporate bonds are valued based on yields currently available on comparable securities of issuers with similar credit ratings. Investments in certain restricted common stocks are valued at the quoted market price of the issuer's unrestricted common stock, less an appropriate discount.

CalPERS' mortgages are valued on the basis of their future principal and interest payments, discounted at prevailing interest rates for similar instruments. The fair value of real estate investments, principally rental property subject to long-term net leases, is estimated based on independent appraisals. Short-term investments are reported at market value, when available, or at cost plus accrued interest, which approximates market value when market value is not available. For investments where no readily ascertainable market value exists, management, in consultation with its investment advisors, has determined the fair values for the individual investments.

Under the State Constitution and statutory provisions governing CalPERS' investment authority, CalPERS, through its outside investment managers, holds investments in futures and options and enters into forward foreign currency exchange contracts. Futures and options with a negative fair value of approximately \$393 million were held for investment purposes as of June 30, 2005. Gains and losses on futures and options are determined based upon quoted market values and recorded in the statement of changes in fiduciary net assets.

Due to the level of risk associated with certain derivative investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the financial statements.

Forward foreign currency exchange contracts are used primarily to hedge against changes in exchange rates related to foreign securities. As of June 30, 2005, CalPERS had approximately a \$393 million net exposure to loss from forward foreign currency exchange transactions related to the approximately \$43.0 billion international debt and equity portfolios. CalPERS could be exposed to risk if the counterparties to the contracts are unable to meet the terms of the contracts. CalPERS investment managers seek to control this risk through counterparty credit evaluations and approvals, counterparty credit limits, and exposure monitoring procedures. CalPERS anticipates that the counterparties will be able to satisfy their obligations under the contracts.

The fair value of investments for CalSTRS is generally based on published market prices and quotations from major investment firms. In the case of debt securities acquired through private placements, management computes fair value based on market yields and average maturity dates of comparable quoted securities. Mortgages are valued based on future principal and interest payments, and are discounted at prevailing interest rates for similar instruments. Real estate equity investment fair values are based on either recent estimates provided by CalSTRS' contract real estate advisors or independent appraisers. Short-term investments are reported at cost or amortized cost, which approximates fair value. Alternative investments

represent interests in private equity partnerships which the system enters into under a limited partnership agreement. For alternative investments and other investments where no readily ascertainable market value exists, CalSTRS management, in consultation with its investment advisors, has determined the fair value for the individual investments. Purchases and sales are recorded on the trade date.

The State Constitution, state statutes, and board policies permit CalPERS and CalSTRS to lend their securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. Third-party securities lending agents are under contract to lend domestic and international equity and debt securities. All securities loans can be terminated on demand by the lender or the borrower. Collateral, in the form of cash or other securities, is required at 102% and 105% of the fair value of domestic and international securities loaned, respectively, for both CalPERS and CalSTRS. As of June 30, 2005, there was no credit risk of exposure to borrowers, because the amount of collateral held exceeded the amounts owed by the borrowers. Collateral securities received are not permitted to be pledged or sold unless the borrower defaults. The contracts with the securities lending agents require them to indemnify CalPERS and CalSTRS if the borrowers fail to return the securities (and if the collateral is not sufficient to replace the securities loaned) or if the borrowers fail to pay for income distributions by the securities' issuers while the securities are on loan.

For CalPERS, the weighted average maturities of the collateral invested by three of its four externally managed and one internally managed portfolios were 349 days, 114 days, 113 days, and 285.39 days. In accordance with CalPERS investment guidelines, the cash collateral was invested in short-term investment funds that, at June 30, 2005, had durations of 44 days, 29 days, 39 days, and 23.74 days, respectively, for three externally managed and one internally managed portfolios. For one externally managed portfolio, the duration of the collateral is matched with the duration of the loan.

For CalSTRS, cash collateral received on each security loan was invested in short-term investments that, at June 30, 2005, had a weighted average maturity of 10 days.

The Regents of the University of California (regents), as the governing board, are responsible for the management of the university's and the UCR's investments and establishes investment policy. For more information about the investment policies of the University of California, refer to section D, Discretely Presented Component Units, below.

Table 6 presents the investments of the fiduciary funds by investment type.

Table 6**Schedule of Investments - Fiduciary Funds**

June 30, 2005

(amounts in thousands)

Investment Type	Fair Value
Equity securities	\$ 227,060,642
Debt securities	111,612,115
Investment contracts	2,514,332
Mutual funds	5,044,601
Real estate	18,204,480
Money market securities	534,683
Insurance contracts	928,098
Private equity	17,446,410
Securities lending collateral	69,652,234
Total investments	\$ 452,997,595

1. Interest Rate Risk

CalPERS, CalSTRS, and UCRS monitor the interest rate risk inherent in their portfolios by measuring the effective duration of the portfolio. Effective duration makes assumptions regarding the most likely timing and amounts of variable cash flows arising from such investments as callable bonds, prepayments, and variable-rate debt. Due to the sophisticated nature of its portfolio, CalPERS uses a weighted average effective duration (WAED) method. WAED weights the effective duration of the groups of investments within an investment type by the dollar size of the individual groups.

Table 7 presents the debt securities of the fiduciary funds by interest rate risk.

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Table 7**Schedule of Debt Securities - Fiduciary Funds - Interest Rate Risk**

June 30, 2005

(amounts in thousands)

	Fair Value at Year End	Effective Duration*			
California Public Employees' Retirement System					
U.S. Treasuries and agencies	\$ 13,106,542	8.32			
Mortgages	18,125,088	3.66			
Corporate	11,361,713	8.76			
Asset-backed	7,230,777	2.54			
International	4,516,658	9.66			
Total	\$ 54,340,778				
University of California Retirement System					
U.S. Treasury bills, notes, and bonds	\$ 2,598,387	2.10			
U.S. Treasury strips	1,919,297	14.00			
U.S. TIPS	2,581,848	4.40			
U.S. government-backed securities	16,696	6.90			
U.S. government-backed asset-backed securities	78,870	2.70			
Corporate bonds	2,809,783	9.10			
Commercial paper	788,560	0.00			
U.S. agencies	3,210,451	3.20			
U.S. agencies asset-backed securities	2,994,743	2.30			
Corporate asset-backed securities	553,811	1.70			
Supranational/foreign	737,758	8.30			
Other	6,918	14.80			
Corporate (foreign currency denominated)	74,037	13.10			
Money market funds	534,683	2.10			
Total	\$ 18,905,842				
California State Teachers' Retirement System					
Long-term fixed income investments					
U.S. Government and agency obligations	\$ 8,066,427	4.97			
Corporate	8,078,651	5.83			
High yield	2,748,841	3.95			
Asset-backed securities	825,092	2.64			
Commercial mortgage-backed securities	860,813	4.39			
Mortgage-backed securities	11,062,286	2.22			
Total	\$ 31,642,110				
Short-term fixed income investments					
Money market securities	\$ 872,765	\$ 112,838	\$ —		
Corporate bonds	—	—	—		
Corporate floating-rate notes	466,713	418,220	27,997		
U.S. Government and agency obligations					
Noncallables	—	—	—		
Discount notes	—	99,737	—		
Callable	8,000	318,987	148,997		
U.S. Treasury	—	—	—		
Asset-backed securities	59,850	73,670	2,850		
Total	\$ 1,407,328	\$ 1,023,452	\$ 179,844		

* Effective duration is described in the paragraph preceding this table.

121-180 days	181-365 days	365+ days	Fair Value at Year End
\$ —	\$ —	\$ —	\$ 985,603
—	4,999	24,972	29,971
—	—	—	912,930
—	50,056	54,707	104,763
—	—	—	99,737
26,500	—	—	502,484
—	75,241	—	75,241
—	19,999	—	156,369
<u>\$ 26,500</u>	<u>\$ 150,295</u>	<u>\$ 79,679</u>	<u>\$ 2,867,098</u>

Table 8 identifies the debt securities that are highly sensitive to interest rate fluctuations (to a greater degree than already indicated in the information provided above).

Table 8**Schedule of Debt Securities – Fiduciary Funds – Interest Rate Risk**

June 30, 2005

(amounts in thousands)

Highly Sensitive Investments	Fair Value at Year End	Effective Duration
University of California Retirement System		
Mortgage Pass-through Securities These securities are issued by the Federal National Mortgage Association (Fannie Mae), Government National Mortgage Association (Ginnie Mae), and Federal Home Loan Mortgage Association (Freddie Mac) and include short embedded prepayment options. Unanticipated prepayments by the obligees of the underlying asset reduce the total expected rate of return.	\$ 3,522,099	1.80
Collateralized Mortgage Obligations Collateralized mortgage obligations (CMO's) generate a return based upon either the payment of interest or principal on mortgages in an underlying pool. The relationship between interest rates and prepayments makes the fair value highly sensitive to changes in interest rates. In falling interest rate environments, the underlying mortgages are subject to a higher propensity of prepayments. In a rising interest rate environment, the opposite is true.	105,325	3.50
Callable Bonds Although bonds are issued with clearly defined maturities, an issuer may be able to redeem or call a bond earlier than its maturity date. The University must then replace the called bond with a bond that may have a lower yield than the original. The call feature causes the fair value to be highly sensitive to changes in interest rates.	880,196	4.00

Table 9 presents the debt securities of the fiduciary funds by credit risk.

Table 9

Schedule of Debt Securities – Fiduciary Funds – Credit Risk

June 30, 2005

(amounts in thousands)

Credit Rating as of Year End		Fair Value
Short-term	Long-term	
A-1+	AAA	\$ 54,089,889
	AAA3	671,139
A-1	AA2/AA	9,026,450
A-2	A2/A	15,451,049
A-3	BAA2/BBB	10,953,632
B	BA2/BB	2,123,437
	B2/B	2,413,621
	CAA2/CCC	613,490
	CA	82,154
	C	301
Not rated		21,003,621
Not applicable		31,591,627
Total debt securities		\$ 148,020,410

2. Concentration of Credit Risk

Concentration of credit risk is the risk association with a lack of diversification. UCRS held \$3.5 billion in Federal agency securities of the Federal National Mortgage Association, which represented 6.91% of UCRS's total investments as of June 30, 2005.

3. Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. CalPERS, CalSTRS, and UCRS held \$45.3 billion, \$23.5 billion, and \$4.2 billion, respectively, in securities subject to foreign currency risk.

Table 10 identifies the investments of the fiduciary funds that are subject to foreign currency risk.

Table 10**Schedule of Investments - Fiduciary Funds - Foreign Currency Risk**

June 30, 2005

(amounts in thousands of U.S. dollars)

Currency	Cash	Equity	Alternative	Fixed Income	Real Estate	Currency Overlay	Total
Argentine Peso	\$ 5	\$ 13	\$ —	\$ —	\$ —	\$ —	\$ 18
Australian Dollar	63,255	2,858,931	3,755	248,237	—	(247)	3,173,931
Brazilian Real	6,606	787,973	—	-	—	—	794,579
British Pound Sterling	365,139	13,943,216	63,506	318,189	—	20,487	14,710,537
Canadian Dollar	12,188	2,189,125	8,861	99,826	9,314	2,524	2,321,838
Chilean Peso	708	61,362	—	—	—	—	62,070
Chinese Yuan	(2)	4,345	—	—	—	—	4,343
Czech Koruna	169	42,944	—	—	—	—	43,113
Danish Krone	12,692	568,336	757	131,352	—	(2,541)	710,596
Euro	396,275	22,261,230	340,905	2,310,824	—	(2,149,551)	23,159,683
Hong Kong Dollar	40,500	1,568,123	—	—	—	2,128	1,610,751
Hungarian Forint	496	164,066	—	10,197	—	—	174,759
Indian Rupee	7,197	231,540	—	—	—	—	238,737
Indonesian Rupiah	535	125,751	—	—	—	—	126,286
Israeli Shekel	1,332	254,766	—	—	—	—	256,098
Japanese Yen	252,500	11,582,184	14,717	1,122,273	—	55,137	13,026,811
Malaysian Ringgit	2,081	243,602	—	—	—	—	245,683
Mexican Peso	4,487	601,668	—	33,770	—	—	639,925
New Zealand Dollar	3,832	264,203	—	—	—	(12)	268,023
Norwegian Krone	6,581	575,975	—	88,179	—	1,298	672,033
Philippine Peso	4	146,277	—	—	—	—	146,281
Polish Zloty	378	84,804	—	76,474	—	—	161,656
Singapore Dollar	2,833	1,065,756	—	34,999	—	63	1,103,651
South African Rand	10,748	790,193	—	—	—	(1,918)	799,023
South Korean Won	825	1,361,022	—	30,676	—	—	1,392,523
Swedish Krona	43,354	1,449,990	—	50,567	—	2,881	1,546,792
Swiss Franc	126,718	3,912,353	371	—	—	(498,846)	3,540,596
Taiwan Dollar	7,969	863,587	—	—	—	—	871,556
Thailand Baht	5,898	184,463	—	—	—	—	190,361
Turkish New Lira	1,912	339,799	—	—	—	—	341,711
Other	—	6,488	—	—	—	—	6,488
Various denominations	—	636,495	—	—	—	—	636,495
Total exposure to foreign currency risk	\$ 1,377,215	\$ 69,170,580	\$ 432,872	\$ 4,555,563	\$ 9,314	\$ (2,568,597)	\$ 72,976,947

D. Discretely Presented Component Units

A portion of the cash and pooled investments of the State Compensation Insurance Fund (SCIF), the California Housing Finance Agency (CalHFA), and nonmajor component units is invested in the State Treasurer's pooled investment program. Additionally, state law, bond resolutions, and investment policy

resolutions allow these component units to invest in U.S. government securities, state and municipal securities, commercial paper, corporate bonds, investment agreements, real estate, and other investments.

The investments of the University of California, a discretely presented component unit, and the UCRS, a pension and other employee benefit trust fund reported in the Fiduciary Fund statements of the primary government, are primarily stated at fair value. Investments authorized by the regents include equity securities, fixed-income securities, and real estate. The equity portion of the investment portfolio may include domestic and foreign common and preferred stocks, and actively managed and passive (index) strategies, along with a modest exposure to private equities. Private equities include venture capital partnerships, buy-outs, and international funds. The fixed-income portion of the investment portfolio may include both domestic and foreign securities, along with certain securitized investments, including mortgage-backed and asset-backed securities. Absolute return strategies, incorporating short sales, plus derivative or option positions to implement or hedge an investment position, are also authorized. Where donor agreements place constraints on allowable investments, assets associated with endowments are invested in accordance with the terms of the agreements.

The University of California participates in a securities lending program as a means to augment income. The university loans securities to select brokerage firms and receives collateral in excess of the fair value of such investments during the period of the loan. Collateral may be cash or securities issued by the U.S. government or its agencies, or the sovereign or provincial debt of foreign countries. Collateral securities cannot be pledged or sold by the university unless the borrower defaults. Loans of domestic equities and all fixed-income securities are initially collateralized at 102% of the fair value of the securities loaned. Loans of foreign equities are initially collateralized at 105%. All borrowers are required to provide additional collateral by the next business day if the value falls to less than 100% of the fair value of the securities loaned. The university earns interest and dividends on the collateral held during the loan period, as well as a fee from the brokerage firm, and is obligated to pay a fee and a rebate to the borrower. The university receives the net investment income. As of June 30, 2005, the university had no credit risk exposure to borrowers, because the amounts the university owed the borrowers exceeded the amounts the borrowers owed the university. The university is fully indemnified by its custodial bank against any losses incurred as a result of borrower default.

Securities loans immediately terminate upon notice by either the university or the borrower. Cash collateral is invested by the university's lending agent in a short-term investment pool in the university's name, with guidelines approved by the university. As of June 30, 2005, the securities in this pool had a weighted average maturity of 30 days.

The State Department of Insurance permits SCIF to lend a certain portion of its securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. A third-party lending agent has been contracted to lend U.S. Treasury notes and bonds. Collateral, in the form of cash and other securities, is adjusted daily and is required at all times to equal at least 100% of the fair value of securities loaned. Collateral securities received are not permitted to be pledged or sold unless the borrower defaults. The maximum loan term is one year. In accordance with SCIF's investment guidelines, cash collateral was invested in short-term investments at December 31, 2004, with maturities matching the related loans. Interest income on these investments is shared by the borrower, the third-party lending agent, and SCIF.

Table 11 presents the investments of the discretely presented component units by investment type.

Table 11**Schedule of Investments – Discretely Presented Component Units**

June 30, 2005

(amounts in thousands)

Investment Type	Fair Value
Equity securities	\$ 5,284,658
Debt securities	27,390,084
Investment contracts	2,660,943
Mutual funds	2,550,171
Real estate	197,981
Money market securities	380,113
Private equity	230,855
Mortgage loans	103,567
Externally held irrevocable trusts	256,977
Repurchase agreements	21,885
Other	(292,018)
Securities lending collateral	3,794,111
Total investments	\$ 42,579,327

1. Interest Rate Risk

Table 12 presents the debt securities of the discretely presented component units by interest rate risk.

Table 12

Schedule of Debt Securities - Discretely Presented Component Units - Interest Rate Risk

June 30, 2005

(amounts in thousands)

Investment Type	University of California		University of California Foundations	
	Fair Value at Year End	Effective Duration	Fair Value at Year End	Effective Duration
U.S. Treasury bills, notes and bonds	\$ 1,648,305	2.80	\$ 127,216	1.30
U.S. Treasury strips	193,062	14.00	—	—
U.S. TIPS	254,419	4.40	—	—
U.S. government-backed securities	4,288	6.90	6,042	3.60
U.S. government-backed asset-backed securities	8,248	2.60	25	0.60
Corporate bonds	1,932,914	2.90	60,524	5.40
Commercial paper	2,910,091	0.00	—	—
U.S. agencies	908,297	1.80	81,354	1.60
U.S. agencies asset-backed securities	247,855	2.30	2,971	0.90
Corporate asset-backed securities	52,820	1.50	3,240	1.60
Supranational/foreign	911,665	2.30	640	2.80
Other	707	8.10	856	2.80
Corporate (foreign currency denominated)	10,423	23.20	—	—
U.S. bond funds	44,799	4.20	228,860	4.10
Non-U.S. bond funds	—	—	14,429	5.00
Money market funds	7,304	0.00	343,260	2.10
Mortgage loans	99,021	0.00	4,546	0.00
Total	\$ 9,234,218		\$ 873,963	

Investment Type	Other Discretely Presented Component Units		California Housing Finance Agency		Public Employees' Benefits Fund	
	Fair Value at Year End	Weighted Average Maturity*	Fair Value at Year End	Effective Duration	Fair Value at Year End	Effective Duration
Securities lending collateral	\$ 928,024	0.04	\$ —	—	\$ —	—
U.S. Treasury and agency securities	4,788,616	3.47	52,779	9.55	224,433	6.79
Municipal securities	491,131	4.74	—	—	—	—
Public utilities	577,792	5.66	—	—	—	—
Corporate bonds	5,280,821	5.27	—	—	187,013	8.67
Commercial paper	—	—	7,456	0.27	—	—
Investment agreements	8,014	0.01	—	—	—	—
Special revenue	651,708	9.85	—	—	—	—
Other government	49,450	3.92	—	—	41,332	6.75
Mortgage-backed securities	4,784,011	5.44	—	—	213,184	2.85
Mutual funds	250,983	0.08	—	—	—	—
Asset-backed	—	—	—	—	45,577	0.45
Sovereign	—	—	—	—	14,830	10.22
Pooled	—	—	—	—	68,645	—
Total	\$ 17,810,550		\$ 60,235		\$ 795,014	

* Weighted Average Maturity does not include the California Housing Finance Agency and the Public Employees' Benefits Fund.

Table 13 identifies the debt securities that are highly sensitive to interest rate fluctuations (to a greater degree than already indicated in the information provided above).

Table 13**Schedule of Debt Securities – Discretely Presented Component Units – Interest Rate Risk**

June 30, 2005

(amounts in thousands)

	University of California		University of California Foundations	
	Fair Value at Year End	Effective Duration	Fair Value at Year End	Effective Duration
Highly Sensitive Investments				
Mortgage Pass-Through Securities	\$ 308,923	2.10	\$ 56,231	1.50
These securities are issued by the Federal National Mortgage Association (Fannie Mae), Government National Mortgage Association (Ginnie Mae) and Federal Home Loan Mortgage Corporation (Freddie Mac) and include short embedded prepayment options. Unanticipated prepayments by the obligees of the underlying asset reduce the total expected rate of return.				
Collateralized Mortgage Obligations			19,944	1.50
Collateralized mortgage obligations (CMO's) generate a return based upon either the payment of interest or principal on mortgages in an underlying pool. The relationship between interest rates and prepayments makes the fair value highly sensitive to changes in interest rates. In falling interest rate environments, the underlying mortgages are subject to a higher propensity of prepayments. In a rising interest rate environment, the opposite is true.				
Other Asset-Backed Securities			2,965	1.70
Other asset-backed securities also generate a return based upon either the payment of interest or principal on obligations in an underlying pool, generally associated with auto loans or credit cards. As with CMO's, the relationship between interest rates and prepayments makes the fair value highly sensitive to changes in interest rates.				
Callable Bonds	22,160	5.20	1,245	1.50
Although bonds are issued with clearly defined maturities, an issuer may be able to redeem, or call, a bond earlier than its maturity date. The university must then replace the called bond with a bond that may have a lower yield than the original. The call feature causes the fair value to be highly sensitive to changes in interest rates.				

Table 14 presents the debt securities of the discretely presented component units by credit risk.

Table 14

Schedule of Debt Securities – Discretely Presented Component Units – Credit Risk

June 30, 2005

(amounts in thousands)

Credit Rating as of Year End		Fair Value
Short-term	Long-term	
A-1+	AAA	\$ 13,476,501
A-1/P-1	AA2/AA	7,093,088
A-2	A2/A	6,028,335
A-3	BAA2/BBB	548,674
B	BA2/BB	125,465
	B2/B	488
Not rated		1,064,961
Not applicable		2,294,384
Total debt securities		\$ 30,631,896

2. Concentration of Credit Risk

Concentration of credit risk is the risk associated with a lack of diversification. Table 15 identifies debt securities in any one issuer (other than U.S. Treasury securities) that represent 5% or more of a discretely presented component unit's investments.

Table 15

Schedule of Debt Securities – Discretely Presented Component Units – Concentration of Credit Risk

June 30, 2005

(amounts in thousands)

Issuer	Investment Type	Reported Amount	% of Total Agency Investments
University of California			
Federal National Mortgage Association	Federal agency securities	\$ 701,673	5.82 %
California Educational Facilities Authority			
Financial Guarantee Insurance Company	Guaranteed investment contract	8,014	78.23
California Infrastructure and Economic Development Bank			
AIG Matched Funding Corporation	Collateralized investment agreements	47,922	100.00

3. Custodial Credit Risk

Custodial credit risk is the risk that in the event of the failure of the custodian, the investments may not be returned. Table 16 presents the debt securities of the discretely presented component units subject to custodial credit risk.

Table 16**Schedule of Debt Securities – Discretely Presented Component Units – Custodial Credit Risk**

June 30, 2005

(amounts in thousands)

Investment Type	Fair Value
University of California Foundations	
Domestic equity securities	\$ 193,151
Foreign equity securities	12,844
U.S. Treasury bills, notes, and bonds	46,302
U.S. government-backed securities	1,604
Corporate bonds	16,467
U.S. agencies	24,033
Corporate asset-backed securities	275
California Educational Facilities Authority	
Guaranteed investment contract	\$ 8,013,594

4. Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. Table 17 identifies the investments of the University of California, including its campus foundations, which are subject to foreign currency risk.

Table 17

Schedule of Investments – Discretely Presented Component Units – Foreign Currency Risk

June 30, 2005

(amounts in thousands)

Currency	Equity	Fixed Income	Total
Australian Dollar	\$ 46,883	\$ —	\$ 46,883
British Pound Sterling	126,415	—	126,415
Canadian Dollar	17,571	10,423	27,994
Danish Krone	37,803	—	37,803
Euro	414,782	—	414,782
Hong Kong Dollar	18,773	—	18,773
Japanese Yen	97,478	—	97,478
New Zealand Dollar	13,261	—	13,261
Norwegian Krone	22,671	—	22,671
Singapore Dollar	125,039	—	125,039
South African Rand	3,124	—	3,124
Swedish Krona	42,814	—	42,814
Swiss Franc	42,756	—	42,756
Other	11,850	—	11,850
Various denominations	273,715	—	273,715
Total exposure to foreign currency risk	\$ 1,294,935	\$ 10,423	\$ 1,305,358

NOTE 4: ACCOUNTS RECEIVABLE

Table 18 presents the disaggregation of accounts receivable attributable to taxes, interest expense reimbursements, Lottery retailer collections, and unemployment program receipts. Other receivables are for interest, gifts, grants, various fees, penalties, and other charges. The adjustment for the fiduciary funds represents amounts due from fiduciary funds that were reclassified as external receivables on the government-wide Statement of Net Assets.

Table 18**Schedule of Accounts Receivable**

June 30, 2005

(amounts in thousands)

	Reimbursement of Accrued					
	Taxes	Interest Expense	Lottery Retailers	Unemployment Programs	Other	Total
Current governmental activities						
General Fund	\$ 7,328,696	\$ —	\$ —	\$ —	\$ 444,810	\$ 7,773,506
Federal Fund	—	—	—	—	6,530	6,530
Transportation Construction Fund	310,523	—	—	—	85,594	396,117
Nonmajor governmental funds	140,900	—	—	—	1,145,961	1,286,861
Internal service funds	—	—	—	—	81,255	81,255
Adjustment:						
Fiduciary funds	—	—	—	—	2,473	2,473
Total current governmental activities	\$ 7,780,119	\$ —	\$ —	\$ —	\$ 1,766,623	\$ 9,546,742
Amounts not scheduled for collection during the subsequent year						
	\$ 1,097,109	\$ —	\$ —	\$ —	\$ —	\$ 1,097,109
Current business-type activities						
Water Resources Fund	—	—	—	—	96,697	96,697
Public Buildings Construction Fund ..	—	127,542	—	—	—	127,542
State Lottery Fund	—	—	152,718	—	—	152,718
Unemployment Programs Fund	—	—	—	143,264	—	143,264
Nonmajor enterprise funds	—	—	—	—	59,285	59,285
Adjustment:						
Account reclassification	—	(127,542)	—	—	(8,258)	(135,800)
Total current business-type activities	\$ —	\$ —	\$ 152,718	\$ 143,264	\$ 147,724	\$ 443,706
Amounts not scheduled for collection during the subsequent year						
	\$ —	\$ —	\$ —	\$ 43,357	\$ —	\$ 43,357

NOTE 5: RESTRICTED ASSETS

Table 19 presents a summary of the legal restrictions placed on assets in the enterprise funds of the primary government and the discretely presented component units.

Table 19**Schedule of Restricted Assets**

June 30, 2005

(amounts in thousands)

	Cash and Pooled Investments	Investments	Due From Other Governments	Loans Receivable	Total
Primary government					
Debt service	\$ 1,529,180	\$ 89,171	\$ 62,434	\$ 627,588	\$ 2,308,373
Construction	213,503	—	—	—	213,503
Operations	1,942,008	—	—	—	1,942,008
Other	18,514	—	—	—	18,514
Total primary government	3,703,205	89,171	62,434	627,588	4,482,398
Discretely presented component units					
Nonmajor component units – debt service.....	147,021	68,700	—	—	215,721
Total discretely presented component units	147,021	68,700	—	—	215,721
Total restricted assets	\$ 3,850,226	\$ 157,871	\$ 62,434	\$ 627,588	\$ 4,698,119

NOTE 6: NET INVESTMENT IN DIRECT FINANCING LEASES

The State Public Works Board, an agency that accounts for its activities as an enterprise fund, has entered into lease-purchase agreements with various other primary government agencies, the University of California, and certain local agencies. Payments from these leases will be used to satisfy the principal and interest requirements of revenue bonds issued by the State Public Works Board.

The minimum lease payments to be received by the State Public Works Board for the primary government are summarized in Table 20.

Table 20
**Schedule of Minimum Lease Payments to Be Received by the State Public Works Board
for the Primary Government**

(amounts in thousands)

Year Ending June 30	Primary Government Agencies	University of California	Local Agencies	Total
2006	\$ 443,176	\$ 125,588	\$ 60,495	\$ 629,259
2007	405,509	124,651	59,912	590,072
2008	403,789	124,882	60,133	588,804
2009	397,145	122,896	59,842	579,883
2010	380,441	115,539	59,055	555,035
2011-2015	1,713,496	570,861	268,082	2,552,439
2016-2020	1,401,341	390,466	111,210	1,903,017
2020-2025	606,453	197,119	9,107	812,679
2026-2030	235,222	50,991	7,278	293,491
2031-2035	3,633	—	—	3,633
Total minimum lease payments	5,990,205	1,822,993	695,114	8,508,312
Less: unearned income	2,250,463	669,858	201,784	3,122,105
Net investment in direct financing leases	\$ 3,739,742	\$ 1,153,135	\$ 493,330	\$ 5,386,207

NOTE 7: CAPITAL ASSETS

Table 21 summarizes the capital activity for the primary government, which includes \$5.0 billion in capital assets related to capital leases.

Table 21**Schedule of Changes in Capital Assets – Primary Government**

June 30, 2005

(amounts in thousands)

	Beginning Balance	Additions	Deductions	Ending Balance
Governmental activities				
Capital assets not being depreciated				
Land	\$ 14,383,694	\$ 351,326	\$ 4,970	\$ 14,730,050
State highway infrastructure	54,467,725	647,157	—	55,114,882
Collections	32,395	1,422	14,463	19,354
Construction in progress	4,783,191	1,836,096	990,824	5,628,463
Total capital assets not being depreciated	73,667,005	2,836,001	1,010,257	75,492,749
Capital assets being depreciated				
Buildings and improvements	14,723,120	841,919	274,996	15,290,043
Infrastructure	377,175	34,283	1,755	409,703
Equipment and other assets	3,918,992	250,889	181,711	3,988,170
Total capital assets being depreciated	19,019,287	1,127,091	458,462	19,687,916
Less accumulated depreciation for:				
Buildings and improvements	4,459,053	549,979	182,888	4,826,144
Infrastructure	119,147	12,237	4,009	127,375
Equipment and other assets	2,860,582	352,925	164,711	3,048,796
Total accumulated depreciation	7,438,782	915,141	351,608	8,002,315
Total capital assets being depreciated, net	11,580,505	211,950	106,854	11,685,601
Governmental activities, capital assets, net	\$ 85,247,510	\$ 3,047,951	\$ 1,117,111	\$ 87,178,350
Business-type activities				
Capital assets not being depreciated				
Land	\$ 23,256	\$ 22,526	\$ —	\$ 45,782
Construction in progress	1,426,442	319,143	132,920	1,612,665
Total capital assets not being depreciated	1,449,698	341,669	132,920	1,658,447
Capital assets being depreciated				
Buildings and improvements	6,450,929	272,054	14,752	6,708,231
Infrastructure	1,205,235	3,023	—	1,208,258
Equipment and other assets	102,595	11,641	32,328	81,908
Total capital assets being depreciated	7,758,759	286,718	47,080	7,998,397
Less accumulated depreciation for:				
Buildings and improvements	2,404,882	141,156	30,570	2,515,468
Infrastructure	657,798	19,253	—	677,051
Equipment and other assets	75,582	8,815	30,559	53,838
Total accumulated depreciation	3,138,262	169,224	61,129	3,246,357
Total capital assets being depreciated, net	4,620,497	117,494	(14,049)	4,752,040
Business-type activities, capital assets, net	\$ 6,070,195	\$ 459,163	\$ 118,871	\$ 6,410,487

Table 22 summarizes the depreciation expense charged to the activities of the primary government.

Table 22**Schedule of Depreciation Expense – Primary Government**

June 30, 2005

(amounts in thousands)

	Amount
Governmental activities	
General government	\$ 72,085
Education	365,005
Health and human services	31,910
Resources	45,213
State and consumer services	34,412
Business and transportation	88,600
Correctional programs	152,726
Internal service funds (charged to the activities that utilize the fund)	125,191
Total depreciation expense – governmental activities	915,142
Business-type activities	
Enterprise	169,224
Total primary government	\$ 1,084,366

Table 23 summarizes the capital activity for discretely presented component units.

Table 23**Schedule of Changes in Capital Assets – Discretely Presented Component Units**

June 30, 2005

(amounts in thousands)

	Beginning Balance	Additions	Deductions	Ending Balance
Capital assets not being depreciated				
Land	\$ 537,897	\$ 60,989	\$ 589	\$ 598,297
Collections	236,478	14,126	159	250,445
Construction in progress	3,066,197 *	362,254	69,019	3,359,432
Total capital assets not being depreciated	3,840,572	437,369	69,767	4,208,174
Capital assets being depreciated				
Buildings and improvements	14,134,230 *	1,542,731	54,327	15,622,634
Equipment and other depreciable assets	7,602,173 *	626,607	687,315	7,541,465
Infrastructure	360,821	6,096	784	366,133
Total capital assets being depreciated	22,097,224	2,175,434	742,426	23,530,232
Less accumulated depreciation for:				
Buildings and improvements	5,269,837 *	549,656	13,741	5,805,752
Equipment and other depreciable assets	5,069,141 *	540,695	636,627	4,973,209
Infrastructure	153,985	11,326	784	164,527
Total accumulated depreciation	10,492,963	1,101,677	651,152	10,943,488
Total capital assets being depreciated, net	11,604,261	1,073,757	91,274	12,586,744
Capital assets, net	\$ 15,444,833	\$ 1,511,126	\$ 161,041	\$ 16,794,918

* Restated

NOTE 8: ACCOUNTS PAYABLE

Accounts payable are amounts due to taxpayers, vendors, customers, beneficiaries, and employees related to different programs. Table 24 presents detail of the accounts payable.

The adjustment for the fiduciary funds represents amounts due to fiduciary funds that were reclassified as external payables on the government-wide Statement of Net Assets.

Table 24

Schedule of Accounts Payable

June 30, 2005

(amounts in thousands)

	Education	Health and Human Services	Resources	Business and Transportation	General Government and Others	Total
Governmental activities						
General Fund	\$ 527,345	\$ 55,338	\$ 87,217	\$ 1,420	\$ 550,191	\$ 1,221,511
Federal Fund	598,126	392,999	58,029	162,084	96,778	1,308,016
Transportation Construction Fund	90	—	—	129,501	7,384	136,975
Nonmajor governmental funds	315,607	554,116	296,574	1,088,693	490,096	2,745,086
Internal service funds	—	71,391	23,106	10,851	72,647	177,995
Adjustment:						
Fiduciary funds	3,157,726	2,994,295	—	37,974	597,952	6,787,947
Total governmental activities	\$ 4,598,894	\$ 4,068,139	\$ 464,926	\$ 1,430,523	\$ 1,815,048	\$ 12,377,530
Business-type activities						
Electric Power Fund	\$ —	\$ —	\$ 424,000	\$ —	\$ —	\$ 424,000
Water Resources Fund	—	—	48,206	—	—	48,206
Public Building Construction Fund	—	—	—	—	4,692	4,692
State Lottery Fund	—	—	—	—	36,193	36,193
Unemployment Program Fund	—	5	—	—	2	7
Nonmajor enterprise funds	16,288	5,825	11	1,566	3,675	27,365
Adjustment:						
Fiduciary funds	—	6,129	—	—	—	6,129
Total business-type activities	\$ 16,288	\$ 11,959	\$ 472,217	\$ 1,566	\$ 44,562	\$ 546,592

NOTE 9: SHORT-TERM FINANCING

As part of its cash management program, the State regularly issues short-term obligations to meet cash flow needs. The State issues revenue anticipation notes (RANs) to partially fund timing differences between revenues and expenditures. A significant portion of the General Fund revenues are received in the latter half of the fiscal year, while disbursements are paid more evenly throughout the fiscal year. If additional external cash flow borrowing is required, the State issues revenue anticipation warrants (RAWs). On October 6, 2004, the State issued \$6.0 billion of RANs, to fund cash flow needs for the 2004-05 fiscal year. The RANs were repaid on June 30, 2005.

The California Housing Finance Agency, a discretely presented component unit, entered into an agreement with a financial institution to provide a line of credit for short-term borrowings of up to \$100 million, which may increase up to \$150 million. At June 30, 2005, draws totaling \$39 million were outstanding.

NOTE 10: LONG-TERM OBLIGATIONS

As of June 30, 2005, the primary government had long-term obligations totaling \$97.4 billion. Of that amount, \$5.0 billion is due within one year, and includes \$494 million in outstanding commercial paper that had been scheduled to be refunded by general obligation bonds issued during the fiscal year. This commercial paper was refunded in July and August 2005. There is an increase in governmental activities general obligation bonds payable because bond sales exceeded redemptions during the year.

The other long-term obligations for governmental activities consist of \$2.8 billion for workers' compensation claims, \$2.3 billion for reimbursement of costs mandated by the State, \$1.4 billion for outstanding debts to schools related to the Proposition 98 funding guarantee, \$1.1 billion for net pension obligations, \$428 million owed for lawsuits, and the University of California unfunded pension liability of \$79 million. The compensated absences will be liquidated by the General Fund, special revenue funds, capital projects funds, and internal service funds. Workers' compensation and capital leases will be liquidated by the General Fund, special revenue funds, and internal service funds. Loans payable, net pension obligations, tax overpayments, Proposition 98 funding guarantee, lawsuits, reimbursement of costs incurred by local agencies and school districts for costs mandated by the State, and the University of California pension liability will be liquidated by the General Fund. The \$548 million in other long-term obligations for business-type activities is mainly for advance collections. These other long-term obligations do not have required payment schedules, or they will be paid when funds are appropriated. The changes in the long-term obligations during the year ended June 30, 2005, are summarized in Table 25.

Table 25

Schedule of Changes in Long-Term Obligations

(amounts in thousands)

	Balance July 1, 2004	Additions	Deductions	Balance June 30, 2005	Due Within One Year	Noncurrent Liabilities
Governmental activities						
Loans payable	\$ 880,226	\$ 131,574	\$ —	\$ 1,011,800	\$ —	\$ 1,011,800
Compensated absences payable ...	1,531,399	875,941	531,237	1,876,103	167,711	1,708,392
Certificates of participation and commercial paper	849,360	2,083,488	2,180,835	752,013	505,512	246,501
Capital lease obligations	3,745,410	414,738	241,588	3,918,560	230,605	3,687,955
General obligation bonds payable ..	43,924,636	2,978,080	1,361,299	45,541,417	1,721,350	43,820,067
Revenue bonds payable	8,101,855	99,250	132,125	8,068,980	91,280	7,977,700
Other long-term obligations	7,740,307	907,766	457,135	8,190,938	605,131	7,585,807
Total	\$ 66,773,193	\$ 7,490,837	\$ 4,904,219	\$ 69,359,811	\$ 3,321,589	\$ 66,038,222
Business-type activities						
Benefits payable	\$ 19,449	\$ —	\$ 2,858	\$ 16,591	\$ —	\$ 16,591
Lottery prizes and annuities	2,460,663	1,944,769	2,058,767	2,346,665	582,496	1,764,169
Compensated absences payable ...	43,200	24,710	23,081	44,829	12,385	32,444
Certificates of participation and commercial paper	97,179	161,970	208,056	51,093	—	51,093
General obligation bonds payable ..	2,215,800	120,000	245,695	2,090,105	126,800	1,963,305
Revenue bonds payable	22,239,016	1,974,919	1,270,399	22,943,536	930,013	22,013,523
Other long-term obligations	564,519	289	17,097	547,711	5,305	542,406
Total	\$ 27,639,826	\$ 4,226,657	\$ 3,825,953	\$ 28,040,530	\$ 1,656,999	\$ 26,383,531

NOTE 11: CERTIFICATES OF PARTICIPATION

Debt service requirements for certificates of participation, which are financed by lease payments from governmental activities, are shown in Table 26. The certificates of participation were used to finance the acquisition and construction of state office buildings.

Table 26

Schedule of Debt Service Requirements for Certificates of Participation – Primary Government

(amounts in thousands)

Year Ending June 30	Principal	Interest	Total
2006	\$ 11,312	\$ 2,893	\$ 14,205
2007	6,579	3,059	9,638
2008	6,292	3,350	9,642
2009	6,099	3,539	9,638
2010	6,042	3,599	9,641
2011-2015	35,574	12,633	48,207
2016-2020	11,915	626	12,541
Total	\$ 83,813	\$ 29,699	\$ 113,512

Debt service requirements for certificates of participation for the University of California, a discretely presented component unit, are shown in Table 27.

Table 27

Schedule of Debt Service Requirements for Certificates of Participation – University of California – Discretely Presented Component Unit

(amounts in thousands)

Year Ending June 30	Principal	Interest	Total
2006	\$ 7,270	\$ 6,766	\$ 14,036
2007	7,640	6,391	14,031
2008	8,020	6,002	14,022
2009	8,490	5,597	14,087
2010	8,980	5,162	14,142
2011-2015	20,010	21,780	41,790
2016-2020	18,245	17,213	35,458
2021-2025	22,270	12,086	34,356
2026-2030	28,775	5,404	34,179
2031-2035	5,520	293	5,813
Total	\$ 135,220	\$ 86,694	\$ 221,914

NOTE 12: COMMERCIAL PAPER AND OTHER LONG-TERM BORROWINGS

The primary government has three commercial paper borrowing programs: a general obligation commercial paper program, an enterprise fund commercial paper program for the Department of Water Resources, and a toll bridges seismic retrofit commercial paper program. Under the general obligation and enterprise fund programs, commercial paper may be issued at prevailing rates for periods not to exceed 270 days from the date of issuance. Under the toll bridges seismic retrofit program, commercial paper may be issued at interest rates determined by the State Treasurer or applicable dealer for period not to exceed 90 days from the date of issuance. The proceeds from the issuance of commercial paper are restricted primarily for construction costs of general obligation bond program projects, certain state water projects, and seismic retrofit projects on State-owned toll bridges. For all three commercial paper borrowing programs, the commercial paper is retired by the issuance of long-term debt, so it is considered a noncurrent liability.

To provide liquidity for the programs, the State has entered into revolving credit agreements with commercial banks. The current agreement for the general obligation commercial paper program, effective December 1, 2004, authorizes the issuance of notes in an aggregate principal amount not to exceed \$1.5 billion. The current agreement for the enterprise fund commercial paper program authorizes the issuance of notes in an aggregate principal amount not to exceed \$141.5 million. The current agreement for the toll bridges seismic retrofit commercial paper program, effective March 1, 2005, authorizes the issuance of notes in an aggregate principal amount not to exceed \$400 million. As of June 30, 2005, the enterprise fund commercial paper program had \$12 million in outstanding notes and the toll bridges seismic retrofit commercial paper program had \$80 million in outstanding notes.

During the year ended June 30, 2005, the primary government issued \$2.0 billion in general obligation commercial paper and \$2.4 billion in long-term general obligation bonds to refund outstanding commercial paper. However, by June 30, 2005, only \$1.9 billion of the \$2.4 billion had been used to repay outstanding commercial paper. The remaining \$494 million was used to repay commercial paper in July and August 2005.

As of June 30, 2005, the general obligation commercial paper program had \$588 million in outstanding commercial paper notes, of which \$494 million is considered a current liability.

The primary government has a revenue bond anticipation note (BAN) program that consists of borrowing for capital improvements on certain campuses of the California State University. As of June 30, 2005, \$39 million in outstanding BANs existed in anticipation of issuing revenue bonds to the public.

The University of California, a discretely presented component unit, has other borrowings consisting of contractual obligations resulting from the acquisition of land or buildings, and the construction and renovation of certain facilities. Included in other borrowings, which total approximately \$311 million, are various unsecured financing agreements with commercial banks that total approximately \$135 million.

The University of California established a \$550 million commercial paper program with tax-exempt and taxable components. The program is supported by the legally available unrestricted investments balance in the University of California's Short-Term Investment Pool. Commercial paper has been issued to provide for interim financing of the construction, renovation, and acquisition of certain facilities and equipment. Commercial paper is secured by a pledge of the net revenues generated by the enterprise financed, not by any encumbrance, mortgage, or other pledge of property, and does not constitute a general obligation of the University of California. At June 30, 2005, outstanding tax-exempt and taxable commercial paper was \$430 million and \$120 million, respectively.

NOTE 13: LEASES

The aggregate amount of lease commitments for facilities and equipment of the primary government in effect as of June 30, 2005, was approximately \$7.1 billion. Primary government leases that are classified as operating leases, in accordance with the applicable standards, contain clauses providing for termination. Operating lease expenditures are recognized as incurred over the lease term. It is expected that, in the normal course of business, most of these operating leases will be replaced by similar leases.

The total present value of minimum capital lease payments for the primary government is composed of \$5 million from internal service funds and \$3.9 billion from other governmental activities. The additions and deductions of capital lease obligations may be found in Note 10, Long-Term Obligations. Also reported in Note 10 are the current and noncurrent portions of the capital lease obligations. Lease expenditures for the year ended June 30, 2005, amounted to approximately \$783 million.

Included in the capital lease commitments are lease-purchase agreements that certain state agencies have entered into with the State Public Works Board, an enterprise fund agency, amounting to a present value of net minimum lease payments of \$3.7 billion. This amount represents 95% of the total present value of minimum lease payments of the primary government. Also included in the capital lease commitments are some lease-purchase agreements to acquire equipment.

The capital lease commitments do not include \$683 million of lease-purchase agreements with building authorities that are blended component units. These building authorities acquire or develop office buildings and then lease the facilities to state agencies. Upon expiration of the lease, title passes to the primary government. The costs of the buildings and the related outstanding revenue bonds and certificates of participation are reported in the government-wide financial statements. Accordingly, the lease receivables or capital lease obligations associated with these buildings are not included in the financial statements.

Future minimum lease commitments of the primary government are summarized in Table 28.

Table 28**Schedule of Future Minimum Lease Commitments – Primary Government**

(amounts in thousands)

Year Ending June 30	Operating Leases	Capital Leases		Total
		Internal Service Funds	Other Governmental Activities	
2006	\$ 243,534	\$ 1,221	\$ 485,425	\$ 730,180
2007	181,879	791	435,714	618,384
2008	136,637	791	429,894	567,322
2009	95,326	794	418,725	514,845
2010	48,621	834	398,277	447,732
2011-2015	108,516	1,599	1,775,347	1,885,462
2016-2020	30,594	—	1,450,151	1,480,745
2021-2025	251	—	639,948	640,199
2026-2030	—	—	235,222	235,222
2031-2035	—	—	3,633	3,633
Total minimum lease payments	\$ 845,358	6,030	6,272,336	\$ 7,123,724
Less: amount representing interest		943	2,358,863	
Present value of net minimum lease payments		\$ 5,087	\$ 3,913,473	

The aggregate amount of discretely presented component units' lease commitments for land, facilities, and equipment in effect as of June 30, 2005, was approximately \$3.4 billion. Table 29 presents the future minimum lease commitments for the University of California and the State Compensation Insurance Fund. Operating lease expenditures for the year ended June 30, 2005, amounted to approximately \$222 million for discretely presented component units.

Table 29

Schedule of Future Minimum Lease Commitments – Discretely Presented Component Units

(amounts in thousands)

Year Ending June 30	University of California		State Compensation Insurance Fund		Total
	Capital	Operating	Operating		
2006	\$ 191,211	\$ 88,361	\$ 47,726	\$	327,298
2007	189,283	73,200	37,524		300,007
2008	182,837	58,668	30,802		272,307
2009	185,916	46,154	20,898		252,968
2010	156,248	30,285	18,741		205,274
2011-2015	762,505	47,311	30,763		840,579
2016-2020	598,901	3,836	—		602,737
2021-2025	404,679	3,540	—		408,219
2026-2030	225,793	3,978	—		229,771
2031-2035	—	4,531	—		4,531
2036-2040	—	4,657	—		4,657
Total minimum lease payments	2,897,373	\$ 364,521	\$ 186,454	\$	3,448,348
Less: amount representing interest	1,013,945				
Present value of net minimum lease payments	\$ 1,883,428				

NOTE 14: COMMITMENTS

As of June 30, 2005, the primary government had commitments of \$4.1 billion for certain highway construction projects. These commitments are not included in the reserve for encumbrances in the Federal Fund and the Transportation Construction Fund because the future expenditures related to these commitments are expected to be reimbursed with \$886 million from local governments and \$3.2 billion in proceeds of approved federal grants. The ultimate liability will not accrue to the State.

The primary government had other commitments totaling \$32.7 billion that are not included as a liability on the Balance Sheet or the Statement of Net Assets. These commitments included \$13.4 billion in long-term contracts to purchase power that are not included as a liability on the Statement of Net Assets of the Electric Power Fund. In addition, there are variable costs, estimated at \$10.6 billion by management, associated with several of the contracts. Purchases will take place in the future, and the commitments will be met with future receipts from charges to residential and commercial energy users. The \$32.8 billion in commitments also included loan and grant agreements that totaled approximately \$6.3 billion to reimburse other entities for construction projects for school building aid, parks, and other improvements. The constructed assets will not belong to the primary government, whose payments are contingent upon the other entities entering into construction contracts.

In addition to the loan and grant commitments, the primary government had commitments of approximately \$1.5 billion for the construction of water projects and the purchase of power, \$1.1 billion for state parks, and \$217 million for the maintenance and operation of the California State Lottery's automated gaming system and its communication systems and services. These are long-term projects, and all needs of the contracts may not have been defined. The projects will be funded with existing and future program resources or with the proceeds of revenue and general obligation bonds.

As of June 30, 2005, the discretely presented component units had other commitments that are not included as a liability on the Statement of Net Assets. The University of California had authorized construction projects

totaling \$3.1 billion. The university has also made commitments to make investments in certain investment partnerships pursuant to provisions in the partnership agreements. These commitments totaled \$1.2 billion as of June 30, 2005. Other component units had outstanding commitments to provide \$628 million for loans under various housing revenue bond programs and \$20 million to other governments for infrastructure improvements.

NOTE 15: GENERAL OBLIGATION BONDS

The State Constitution permits the primary government to issue general obligation bonds for specific purposes and in such amounts as approved by a two-thirds majority of both houses of the Legislature and by a majority of voters in a general or direct primary election. The debt service for general obligation bonds is appropriated from the General Fund. Under the State Constitution, the General Fund is used first to support the public school system and public institutions of higher education; it can then be used to service the debt on outstanding general obligation bonds. Enterprise funds and certain other funds reimburse the General Fund for any debt service provided on their behalf. General obligation bonds that are directly related to, and expected to be paid from, the resources of enterprise funds are included as a liability of such funds in the financial statements. However, the General Fund may be liable for the payment of any principal and interest on these bonds that is not met from the resources of such funds.

As of June 30, 2005, the State had \$45.5 billion in outstanding general obligation bonds related to governmental activities and \$2.1 billion related to business-type activities. In addition, \$35.2 billion of general obligation bonds had been authorized but not issued. This amount includes \$19.8 billion that has been authorized by the applicable finance committee for future issuance in the form of commercial paper notes. Of this amount, \$588 million in general obligation indebtedness has been issued in the form of commercial paper notes but not yet retired by long-term bonds.

Information on the change to general obligation bonds payable can be found in Note 10, Long-Term Obligations.

A. Variable-Rate General Obligation Bonds

As part of the *Strategic Debt Management Plan* adopted in the 2001-02 fiscal year, the State has issued variable-rate general obligation bonds. Prior to the 2004-05 fiscal year, the State had \$1.4 billion of variable-rate general obligation bonds outstanding consisting of \$250 million in daily rate, \$650 million in weekly rate, and \$500 million in auction rate. On October 20, 2004, the State sold an additional \$1.0 billion of variable-rate general obligation bonds consisting of \$590 million in daily rate and \$410 million in weekly rate.

The interest rates associated with the daily rates and weekly rates are determined by the remarketing agents to be the lowest rate that would allow the bonds to sell on the effective date of such rate at a price (without regard to accrued interest) equal to 100% of the principal amount. The interest is paid on the first business day of each calendar month. The interest rates on the auction-rate bonds are determined by the auction agent through an auction process and the interest is paid on the business day immediately following each auction rate period.

Letters of credit were issued to secure payment of principal and interest on the daily and weekly variable-rate bonds. Under these letters of credit, the credit providers pay all principal and interest payments to the bondholders; the State is then required to reimburse the credit providers for the amounts paid. There are different credit providers for each series of variable-rate bonds issued. For the variable-rate bonds issued prior to the 2004-05 fiscal year, the initial expiration dates of the letters of credit for the daily and weekly

variable-rate bonds are April 14, 2008, and April 14, 2006, respectively. For the variable-rate bonds issued during the 2004-05 fiscal year, the initial expiration date of the letters of credit is October 20, 2009.

Sinking fund deposits for the variable-rate general obligation bonds will be set aside in a mandatory sinking fund at the beginning of each fiscal year, starting in the 2015-16 fiscal year and continuing to the 2033-34 fiscal year, based on the schedules provided in the Official Statements. The deposits set aside in any fiscal year, with approval of the State Treasurer and the appropriate bond finance committees, may be applied to the redemption of any other general obligation bonds then outstanding. To the extent that the deposit is not applied by January 31 of each fiscal year, the variable-rate general obligation bonds will be redeemed in whole or in part on an interest payment date in that fiscal year.

B. Economic Recovery Bonds

On March 2, 2004, voters approved the one-time issuance of up to \$15 billion of Economic Recovery Bonds and during the 2003-04 fiscal year, the State sold a total of \$10.9 billion of these bonds. The debt service for these bonds is payable from and secured by amounts available in the Fiscal Recovery Fund, a special revenue fund, that consists primarily of revenues from a dedicated sales tax. However, the General Fund may be liable for the payment of any principal and interest on the bonds that cannot be paid from the Fiscal Recovery Fund.

As of June 30, 2005, the State still had \$10.9 billion of Economic Recovery Bonds outstanding. Of the \$10.9 billion outstanding, bonds totaling \$3.0 billion are variable rate bonds, consisting of \$1.0 billion in daily rate and \$2.0 billion in weekly rate. The interest rates associated with the daily rates and weekly rates are determined by the remarketing agents to be the lowest rate that would enable them to sell the bonds for delivery on the effective date of such rate at a price (without regard to accrued interest) equal to 100% of the principal amount. The interest is paid on the first business day of each calendar month. As described in the Official Statement, payment of principal, interest, and purchase price upon tender, for a portion of these bonds, is secured by a direct-pay letter of credit. Payment of principal and interest for another portion of these bonds is secured by a bond insurance policy, together with an insured standby bond purchase agreement upon tender. A separate uninsured standby bond purchase agreement supports the purchase upon tender for the final portion of these bonds, without credit enhancement in the form of an insurance policy or letter of credit related to the payment of principal or interest. The State reimburses its credit providers for any amounts paid, plus interest. There are different credit providers for each series of variable-rate bonds issued. The initial expiration dates for these letters of credit, bond insurance policies, and standby bond purchase agreements are between June 15, 2007, and December 31, 2015.

Another \$1.0 billion of the \$10.9 billion Economic Recovery Bonds outstanding have interest-reset dates of either July 1, 2007, or July 1, 2008. At that time, the bonds are subject to mandatory tender for purchase at a price equal to 100% of the principal amount, plus accrued interest, without premium. Upon mandatory tender, the State will seek to remarket these bonds. The debt service requirements published in the Official Statement differ from the calculation included in Table 15, because the statement presumes a successful remarketing at an interest rate of 3.33% per year, along with the creation of a mandatory sinking fund. The debt service calculation in Table 15 uses the interest rates in effect at year-end, which are the same interest rates in effect until the applicable reset date, and does not assume the future establishment of a sinking fund. In the event of a failed remarketing, the State is required to return all tendered bonds to their initial purchasers and pay an annual interest rate of 11%, until there is a successful remarketing of these bonds.

C. Debt Service Requirements

Table 30 shows the debt service requirements for all general obligation bonds as of June 30, 2005. The estimated debt service requirements for the \$2.4 billion variable-rate general obligation bonds and the \$3.0 billion variable-rate Economic Recovery Bonds are calculated using the actual interest rates in effect on June 30, 2005.

Table 30**Schedule of Debt Service Requirements for General Obligation Bonds**

(amounts in thousands)

Year Ending June 30	Governmental Activities			Business-type Activities		
	Principal	Interest	Total	Principal	Interest	Total
2006	\$ 1,721,350	\$ 2,153,745	\$ 3,875,095	\$ 126,800	\$ 117,283	\$ 244,083
2007	1,729,850	2,063,487	3,793,337	129,360	106,440	235,800
2008	1,923,362	1,974,518	3,897,880	136,430	96,618	233,048
2009	2,050,965	1,873,942	3,924,907	135,340	86,830	222,170
2010	2,168,750	1,765,175	3,933,925	118,190	77,557	195,747
2011-2015	8,677,600	7,274,192	15,951,792	502,750	305,517	808,267
2016-2020	8,580,120	5,241,286	13,821,406	481,080	176,307	657,387
2021-2025	8,425,260	3,508,387	11,933,647	172,210	98,649	270,859
2026-2030	6,829,030	1,768,829	8,597,859	143,720	58,973	202,693
2031-2035	3,435,130	354,977	3,790,107	128,225	17,201	145,426
2036-2040	—	—	—	16,000	858	16,858
Total	\$ 45,541,417	\$ 27,978,538	\$ 73,519,955	\$ 2,090,105	\$ 1,142,233	\$ 3,232,338

D. General Obligation Bond Defeasances**1. Current Year**

On February 16, 2005, the primary government issued \$794 million in various-purpose general obligation refunding bonds to current and advance refund \$804 million in general obligation bonds maturing in 2009 and 2012 to 2029. The primary government placed the net proceeds into an irrevocable trust to pay the debt service on the refunded bonds. As a result, the refunded bonds are considered defeased and the liability for those bonds has been removed from the financial statements. The refunding decreased overall debt service payments by \$118 million and resulted in an economic gain of \$75 million. The economic gain is the difference between the present value of the old debt service requirements and the present value of the new debt service requirements, discounted at 4.1% per year over the life of the new bonds.

On April 6, 2005, the primary government issued \$764 million in various-purpose general obligation refunding bonds to advance refund \$752 million in general obligation bonds maturing in 2011 to 2030. The primary government placed the net proceeds into an irrevocable trust to pay the debt service on the refunded bonds. As a result, the refunded bonds are considered to be defeased and the liability for those bonds has been removed from the financial statements. This advance refunding reduced debt service payments by \$74 million and resulted in an economic gain of \$46 million, using a discount rate of 4.3%.

On April 12, 2005, the primary government issued \$221 million in veterans general obligation bonds, the proceeds of which were used to immediately refund \$101 million in outstanding general obligation bonds maturing in years 2011 to 2018. This refunding reduced debt service payments by \$14 million and resulted in an economic gain of \$9 million, using a discount rate of 3.0%.

On June 16, 2005, the primary government issued \$380 million in various-purpose general obligation refunding bonds to advance refund \$380 million in general obligation bonds maturing in 2014 to 2029. The primary government placed the net proceeds into an irrevocable trust to pay the debt service on the refunded bonds. As a result, the refunded bonds are considered to be defeased and the liability for those bonds has been removed from the financial statements. This advance refunding reduced debt service payments by \$34 million and resulted in an economic gain of \$21 million, using a discount rate of 4.2%.

2. Prior Years

In prior years, the primary government placed the proceeds of the refunding bonds in a special irrevocable escrow trust account with the State Treasury to provide for all future debt service payments on defeased bonds. The assets of the trust accounts and the liability for defeased bonds are not included in the State's financial statements. As of June 30, 2005, the outstanding balance of general obligation bonds defeased in prior years was approximately \$741 million.

NOTE 16: REVENUE BONDS

A. Governmental Activities

The California Infrastructure and Economic Development Bank is authorized by state law to issue Bay Area Toll Bridges Seismic Retrofit Revenue Bonds. The purpose of these bonds is to finance a portion of the seismic retrofitting of some of the toll bridges owned by the State that serve the Bay Area. These bonds are secured and payable from a \$1 per vehicle seismic surcharge from all toll-paying vehicular traffic on the Bay Area bridges. The State Treasurer is authorized by state law to issue Federal Highway Grant Anticipation Revenue Vehicles (GARVEE bonds). The purpose of these bonds is to accelerate the funding and construction of critical transportation infrastructure projects in order to provide congestion relief benefits to the public significantly sooner than traditional funding mechanisms. These bonds are secured and payable from the annual federal appropriation for the State's federal-aid transportation projects. The primary government has no legal liability for the payment of principal and interest on these revenue bonds. Both of these bonds fund activities in the Transportation Construction Fund and are included in the governmental activities column of the government-wide Statement of Net Assets.

The California State University, Channel Islands Financing Authority, a blended component unit in the California State University Programs Fund, issues revenue bonds to provide funding for public capital improvements serving the California State University, Channel Islands. These bonds are secured and payable from special taxes, tax increment revenues, and pledged rental housing revenues of the California State University, Channel Islands Site Authority, which is also a blended component unit in the California State University Programs Fund. The primary government has no legal liability for the payment of principal and interest on these revenue bonds. The bonds are included in the governmental activities column of the government-wide Statement of Net Assets.

The Golden State Tobacco Securitization Corporation (GSTSC), a blended component unit, is authorized by state law to issue asset-backed bonds to purchase the State's rights to future revenues from the Master Settlement Agreement with participating tobacco companies. These bonds are secured by and payable solely from future Tobacco Settlement Revenue. The primary government has no legal liability for the payment of principal and interest on these bonds. These bonds are included in the governmental activities column of the government-wide Statement of Net Assets.

Under state law, certain building authorities may issue revenue bonds. These bonds are issued for the purpose of acquiring and constructing buildings for public education purposes and for the purpose of constructing state office buildings. Leases with state agencies pay the principal and interest on the revenue bonds issued by the building authorities. The primary government has no legal liability for the payment of principal and interest on these revenue bonds. These revenue bonds are included in the governmental activities column of the government-wide Statement of Net Assets.

B. Business-type Activities

Revenue bonds that are directly related to, and expected to be paid from, the resources of enterprise funds are included in the accounts of such funds. Principal and interest on revenue bonds are payable from the pledged revenues of the respective funds of agencies that issued the bonds. The General Fund has no legal liability for payment of principal and interest on revenue bonds.

Revenue bonds to acquire, construct, or renovate state facilities or to refund outstanding revenue bonds in advance of maturity are issued for water resources, public building construction, and certain nonmajor enterprise funds. Revenue bonds were used to repay advances from the General Fund and loans from financial institutions that were used to finance electric power purchases for resale to utility customers.

C. Discretely Presented Component Units

The University of California issues revenue bonds to finance the construction, renovation, and acquisition of certain facilities and equipment.

Under state law, the California Housing Finance Agency (CalHFA) issues fixed- and variable-rate revenue bonds to make loans to finance housing developments and to finance the acquisition of homes by low- and moderate-income families. Variable-rate debt is typically tied to a common index, such as the Bond Market Association (BMA) or the London Interbank Offered Rate (LIBOR) and is reset periodically.

Table 31 shows revenue bonds outstanding of the primary government and the discretely presented component units.

Table 31

Schedule of Revenue Bonds Outstanding

June 30, 2005

(amounts in thousands)

Primary government	
Governmental activities	
Transportation Construction Fund	\$ 1,733,740
Nonmajor governmental funds	
California State University Programs Fund	195,525
Golden State Tobacco Securitization Corporation Fund	5,456,205
Building authorities	683,510
Total governmental activities	8,068,980
Business-type activities	
Electric Power Fund	10,982,000
Water Resources Fund	2,425,201
Public Building Construction Fund	6,697,293
Nonmajor enterprise funds	2,839,042
Total business-type activities	22,943,536
Total primary government	31,012,516
Discretely presented component units	
University of California	5,065,850
California Housing Finance Agency	7,500,766
Nonmajor component units	508,765
Total discretely presented component units	13,075,381
Total	\$ 44,087,897

Table 32 shows the debt service requirements for fixed- and variable-rate bonds. It excludes certain unamortized refunding costs, premiums, discounts, and other costs that are included in Table 31.

Table 32**Schedule of Debt Service Requirements for Revenue Bonds**

(amounts in thousands)

Year Ending June 30	Primary Government				Discretely Presented Component Units	
	Governmental Activities		Business-type Activities		Principal	Interest*
	Principal	Interest	Principal	Interest*		
2006	\$ 91,280	\$ 452,127	\$ 892,872	\$ 1,026,069	\$ 1,227,505	\$ 450,622
2007	112,305	449,206	889,089	986,526	308,846	422,528
2008	177,220	444,301	929,558	945,198	344,018	407,833
2009	139,895	438,247	985,429	906,588	364,086	391,677
2010	144,635	431,900	1,004,080	861,189	407,049	376,154
2011-2015	726,760	2,054,761	5,613,476	3,514,833	1,919,507	1,600,157
2016-2020	624,280	1,897,144	6,571,716	2,057,603	2,065,685	1,184,756
2021-2025	846,155	1,723,048	3,903,378	816,985	2,002,792	816,297
2026-2030	1,033,110	1,605,192	1,555,993	266,250	2,071,970	483,822
2031-2035	1,468,745	1,310,272	280,760	43,565	1,614,728	209,035
2036-2040	1,811,140	829,695	47,112	1,789	585,503	47,090
2041-2045	893,455	187,972	—	—	12,960	403
Total	\$ 8,068,980	\$ 11,823,865	\$ 22,673,463	\$ 11,426,595	\$ 12,924,649	\$ 6,390,374

*Includes interest on variable-rate bonds based on rates in effect on June 30, 2005.

Table 33 shows debt service requirements as of June 30, 2005, for variable-rate debt included in Table 32, as well as net swap payments, assuming that current interest rates remain the same for their term. As interest rates vary, variable-rate bond interest payments and net swap payments will vary.

Table 33**Schedule of Debt Service and Swap Requirements for Variable-Rate Revenue Bonds**

(amounts in thousands)

Year Ending June 30	Primary Government Business-type Activities				Discretely Presented Component Units			
	Principal	Interest*	Interest Rate* Swap		Principal	Interest*	Interest Rate* Swap	
			Net	Total			Net	Total
2006	\$ —	\$ 33,000	\$ 14,000	\$ 47,000	\$ 79,210	\$ 108,052	\$ 93,030	\$ 280,292
2007	—	33,000	14,000	47,000	94,395	110,471	93,410	298,276
2008	—	33,000	14,000	47,000	112,845	105,235	89,099	307,179
2009	—	33,000	14,000	47,000	118,250	99,242	83,306	300,798
2010	—	33,000	14,000	47,000	121,475	92,904	77,157	291,536
2011-2015	1,026,000	119,000	55,000	1,200,000	664,890	377,791	310,255	1,352,936
2016-2020	404,000	14,000	7,000	425,000	813,355	250,123	205,324	1,268,802
2021-2025	—	—	—	—	918,975	156,590	129,982	1,205,547
2026-2030	—	—	—	—	1,031,060	83,404	71,200	1,185,664
2031-2035	—	—	—	—	816,385	27,226	23,152	866,763
2036-2040	—	—	—	—	98,925	2,409	2,153	103,487
Total	\$ 1,430,000	\$ 298,000	\$ 132,000	\$ 1,860,000	\$ 4,869,765	\$ 1,413,447	\$ 1,178,068	\$ 7,461,280

*Based on rates in effect on June 30, 2005.

D. Primary Government Variable Rate/Swap Disclosure

Objective: The Department of Water Resources (DWR) entered into interest-rate swap agreements with various counterparties to reduce variable-interest-rate risk for the Electric Power Fund. The swaps create a synthetic fixed rate. DWR agreed to make fixed-rate payments and receive floating-rate payments on notional amounts equal to a portion of the principal amount of this variable-rate debt.

Terms and Fair Value: The terms and fair value of the swap agreements entered into by DWR, all of which became effective February 13, 2003, are summarized in Table 34. The notional amounts of the swaps match the principal amounts of the associated debt. The swap agreements contain scheduled reductions to outstanding notional amounts that follow scheduled amortization of the associated debt. Most swaps had a negative fair value as of June 30, 2005, because interest rates had declined. The fair values were provided by the counterparties using the par value or the marked-to-market method.

Credit Risk: As of June 30, 2005, DWR was not exposed to significant credit risk because the swaps had negative fair values. However, should interest rates increase and the fair values become positive, DWR would be exposed to credit risk in the amount of the swaps' fair value. DWR has a total of nine swap agreements with six different counterparties. Three swaps, approximating 35% of the total notional value, are with a counterparty that has Moody's Investors Service, Fitch Ratings, and Standard & Poor's (S&P) credit ratings of Aaa, AAA, and AAA, respectively. Of the remaining swaps, two are held with a single counterparty and approximate 21% of the outstanding notional value; that counterparty has Moody's, Fitch's, and S&P's credit

ratings of Aa3, AA-, and A+, respectively. The remaining four swaps are with separate counterparties, all having Moody's, Fitch's, and S&P's credit ratings of Aa3, A+, and A+, respectively, or better. The credit ratings of the counterparties for the swap agreements are summarized in Table 34.

Table 34**Schedule of Terms, Fair Values, and Credit Ratings of Swap Agreements**

(amounts in thousands)

Swap Termination Date	Outstanding Notional Amount at June 30, 2005	Fair Values at June 30, 2005	Fixed Rate Paid by Electric Power Fund	Variable Rate Received by Electric Power Fund	Counterparty Credit Ratings (Moody's, Fitch's, S&P's)
5/1/2011	\$ 94,000	\$ (3,000)	2.914 %	67% of LIBOR	Aaa, AAA, AAA
5/1/2012	234,000	(6,000)	3.024	67% of LIBOR	Aaa, AAA, AAA
5/1/2013	200,000	(3,000)	3.405	BMA	Aa3, A+, A+
5/1/2013	100,000	(1,000)	3.405	BMA	Aa3, AA-, A+
5/1/2013	30,000	—	3.405	BMA	Aa3, AA-, A+
5/1/2014	194,000	(5,000)	3.204	67% of LIBOR	Aa1, AA-, AA-
5/1/2015	174,000	(9,000)	3.280	67% of LIBOR	Aaa, AAA, AAA
5/1/2016	202,000	(8,000)	3.342	67% of LIBOR	Aa2, AA, AA
5/1/2017	202,000	(9,000)	3.389	67% of LIBOR	Aa3, AA-, A+
Total	\$ 1,430,000	\$ (44,000)			

Basis Risk: DWR is exposed to basis risk on the swaps that have payments calculated on the basis of a percentage of LIBOR. The basis risk results from the fact that DWR's floating interest payments payable on the underlying debt are determined in the tax-exempt market, while the DWR floating receipts on the swaps are based on LIBOR, which is determined in the taxable market. Should the relationship between LIBOR and the tax-exempt market change and move to convergence, or should DWR's bonds trade at levels worse (higher in rate) in relation to the tax-exempt market, DWR's cost would increase. As of June 30, 2005, the variable rate on DWR's bonds ranged from 2.1% to 2.5%, while 67% of LIBOR received on the swap was equal to 2.2%.

Termination Risk: DWR's swap agreements do not contain any out-of-the-ordinary termination events that would expose it to significant termination risk. In keeping with market standards, DWR or the counterparty may terminate a swap agreement if the other party fails to perform under the terms of the contract or in the event of a significant loss of creditworthiness by the other party. DWR views the likelihood of such an event to be remote at this time. If a termination were to occur, at the time of the termination DWR would be liable for payment equal to the swap's fair value, if it had a negative fair value at that time. A termination would mean that DWR's underlying floating-rate bonds would no longer be hedged and DWR would be exposed to floating rate risk, unless it entered into a new hedge.

Rollover Risk: Other than termination, there is no rollover risk associated with the swap agreements, because the agreements have termination dates and notional amounts that are tied to equivalent maturity dates and principal amounts of amortizing debt.

E. Discretely Presented Component Unit Variable Rate/Swap Disclosure – University of California

Table 33 includes debt service requirements and net swap payments as of June 30, 2005, of the University of California (UC), a discretely presented component unit. Total principal, variable interest, and interest rate net swap payments are \$343 million, \$85 million, and \$50 million, respectively.

Objective: UC has entered into interest rate swap agreements as a means to lower borrowing costs, compared to fixed-rate bonds at the time of issuance, and to effectively change the variable interest rate on bonds to a fixed rate of 3.1%. The swaps are with three financial institutions in connection with variable-rate refunding revenue bonds associated with the UC Davis Medical Center.

Terms: The bonds and related swap agreements mature on September 1, 2026. The aggregate notional amount of swaps matches the outstanding amounts on the bonds throughout the term of the bonds. UC pays the swap counterparties a fixed payment of 3.1% and receives a variable payment computed as 67% of the 30-day LIBOR. UC believes that, over time, the variable interest rates it pays on the bonds will approximate the variable payments it receives on the interest rate swaps, leaving the fixed interest rate payment on the swaps as the net payment obligation for the transaction.

Fair Value: The swaps have an estimated negative fair value of \$5.5 million as of June 30, 2005, because interest rates have decreased since the execution of the swaps. The fair value is an indication of the difference in value of the swap fixed-interest payments due and the fixed-rate payments due on a swap with identical terms executed on June 30, 2005. The fair value of the interest rate swap is the estimated amount the UC would have paid if the swap agreement had been terminated on June 30, 2005. The fair value was estimated by the financial institutions using available quoted market prices or a forecast of expected discounted future cash flows.

Basis Risk: UC is exposed to basis risk whenever the interest rates on the bonds are reset. The interest rates on the bonds are tax-exempt interest rates reset weekly or daily, while the variable receipt rate on the interest rate swaps is taxable (67% of the 30-day LIBOR).

Termination and Interest Rate Risk: UC is exposed to losses in the event of nonperformance by counterparties or unfavorable interest rate movements. The swap may be terminated if the insurer's credit quality rating falls below A- as issued by Fitch Ratings or Standard & Poor's, thereby canceling the synthetic interest rate and returning the interest rate payments to the variable interest rates on the bonds. At termination, UC may also owe a termination payment if there is a realized loss on the fair value of the swap.

F. Discretely Presented Component Unit Variable Rate/Swap Disclosure – California Housing Finance Agency

Table 33 includes debt service requirements and net swap payments as of June 30, 2005, for the California Housing Finance Agency (CalHFA), a discretely presented component unit. Total principal, variable interest, and interest rate net swap payments are \$4.5 billion, \$1.3 billion, and \$1.1 billion, respectively.

Objective: CalHFA has entered into interest rate swap agreements with various counterparties to protect itself against rising rates by providing a synthetic fixed rate for a like amount of variable-rate bond obligations. The majority of CalHFA's interest rate swap transactions are structured to pay a fixed rate of interest while receiving a variable rate of interest, with some exceptions. CalHFA previously entered into swaps at a ratio of 65% of LIBOR. Its current formula (60% of LIBOR plus a spread, currently .26%) results in comparable fixed-rate economics but performs better when short-term rates are low and the BMA/LIBOR percentage is high.

CalHFA has used this new formula since December 2002, and it expects to continue to use this formula for LIBOR-based swaps exclusively. In addition, CalHFA entered into 13 basis swaps as a means to change the variable-rate formula received from counterparties for \$667 million outstanding notional amount from 65% of LIBOR to varying floating rates.

Terms, Fair Value, and Credit Risk: Most of CalHFA's notional amounts of the swaps match the principal amounts of the associated debt. CalHFA has created a synthetic fixed rate by swapping a portion of its variable rate debt. CalHFA did not pay or receive any cash when the swap transactions were initiated. CalHFA utilizes ten counterparties for its interest rate swap transactions. Counterparties are required to collateralize their exposure to CalHFA when their credit ratings fall from AA to the highest single-A category, A1/A+. CalHFA is not required to provide collateralization until its ratings fall to the mid-single-A category, A2/A. CalHFA's swap portfolio has an aggregate negative fair value, due to a decline in interest rates, of \$304 million as of June 30, 2005. Fair values are as reported by CalHFA's counterparties and are estimated using the zero-coupon method. Since CalHFA's swap portfolio has an aggregate negative fair value, CalHFA is not exposed to credit risk. However, if interest rates rise the negative fair value of the swap portfolio would be reduced and could eventually become positive. At this point, CalHFA would become exposed to the counterparties' credit, because the counterparties would be obligated to make payments to CalHFA in the event of termination. CalHFA has 117 swap transactions, with outstanding notional amounts of \$4.6 billion. Standard & Poor's credit ratings for these counterparties range from A+ to AAA; Moody's credit ratings range from Aa3 to Aaa.

Basis Risk: CalHFA's swaps contain the risk that the floating-rate component of the swap will not match the floating rate of the underlying bonds. This risk arises because floating rates paid by swap counterparties are based on indices that consist of market-wide averages, while interest paid on CalHFA's variable-rate bonds is specific to individual issues. CalHFA's variable-rate tax-exempt bonds trade at a slight discount to the BMA index. Swaps associated with tax-exempt bonds, for which CalHFA receives a variable-rate payment, are based on a percentage of LIBOR; thus, CalHFA is exposed to basis risk if the relationship between BMA and LIBOR converges. As of June 30, 2005, the BMA rate was 2.28%, 65% of the one-month LIBOR was 2.17%, and 60% of the one-month LIBOR plus 26 basis points was 2.26%.

Termination Risk: Counterparties to CalHFA's interest rate swaps have termination rights that require settlement payments by either CalHFA or the counterparties, based on the fair value of the swap. As of June 30, 2005, termination events occurred which required settlement payments by CalHFA totaling \$602,000.

Rollover Risk: CalHFA's swap agreements have limited rollover risk because the agreements contain scheduled reductions to outstanding notional amounts that are expected to follow scheduled and anticipated reductions in the associated bonds payable.

G. Revenue Bond Defeasances

1. Current Year

In January 2005, the primary government issued \$272 million in Central Valley Project Water System Revenue Bonds, of which a portion of the proceeds were used to refund \$251 million of outstanding bonds. The current refunding resulted in the recognition of an accounting loss of approximately \$18 million for fiscal year 2005. The primary government used the issuance of the Series AC bonds to provide debt service savings of more than \$18 million over the next 23 years, with a net present value of \$12 million.

In June 2004 and November 2004, CalHFA, a discretely presented component unit, issued Multifamily Housing Revenue Bonds. The loss from the debt refunding was deferred and will be amortized as a component of interest expense over the shorter of the term of bonds extinguished or the term of the refunding bonds. The refunding will decrease the debt service cash outflow for Multifamily Programs by approximately \$15 million. The refunding may also provide for an economic gain for the Multifamily Programs, which is estimated to be approximately \$10 million.

2. Prior Years

In prior years, the primary government defeased certain bonds by placing the proceeds of new bonds in irrevocable trust accounts to provide for all future debt service requirements. Accordingly, the assets and liabilities for these defeased bonds are not included in the financial statements. As of June 30, 2005, the outstanding balance of revenue bonds defeased in prior years was approximately \$567 million.

In prior years, the University of California, a discretely presented component unit, defeased certain bonds. Investments that have maturities and interest rates sufficient to fund retirement of defeased liabilities are being held in irrevocable trusts for the debt service payments. Accordingly, the assets of the trust accounts and the liabilities for the defeased bonds are not included in the State's financial statements. As of June 30, 2005, the outstanding balance of University of California revenue bonds defeased in prior years was \$306 million.

NOTE 17: INTERFUND BALANCES AND TRANSFERS**A. Interfund Balances**

Due from other funds and due to other funds represent short-term interfund receivables and payables resulting from the time lag between the dates that goods and services are provided and received and the dates that payments between entities are made. Table 35 presents the amounts due from and due to other funds.

Table 35**Schedule of Due From Other Funds and Due To Other Funds**

June 30, 2005

(amounts in thousands)

Due From	Due To					
	General Fund	Federal Fund	Transportation Construction Fund	Nonmajor Governmental Funds	Electric Power Fund	Water Resources Fund
Governmental funds						
General Fund.....	\$ —	\$ —	\$ 73,587	\$ 1,325,374	\$ —	\$ —
Federal Fund.....	453,297	—	1,016,619	427,810	—	—
Transportation Construction Fund ..	—	—	—	27,101	—	—
Nonmajor governmental funds	104,973	—	7,202	281,009	—	—
Total governmental funds	558,270	—	1,097,408	2,061,294	—	—
Enterprise funds						
Water Resources Fund	—	—	—	—	—	—
Public Building Construction Fund	18,113	—	—	—	—	—
State Lottery Fund.....	228	—	—	279,531	—	—
Unemployment Programs Fund	132,129	—	—	70,695	—	—
Nonmajor enterprise funds	54,378	—	12,466	231	—	—
Total enterprise funds	204,848	—	12,466	350,457	—	—
Internal service funds	1,102	85	19,601	109,655	26,000	3,060
Fiduciary funds	746	—	—	61	—	—
Total primary government	\$ 764,966	\$ 85	\$ 1,129,475	\$ 2,521,467	\$ 26,000	\$ 3,060

Due To						
Public Building Construction Fund	State Lottery Fund	Unemployment Programs Fund	Nonmajor Enterprise Funds	Internal Service Funds	Fiduciary Funds	Total
\$ —	\$ 3,675	\$ —	\$ —	\$ 103,081	\$ 3,749,505	\$ 5,255,222
—	—	2,459	—	57,750	2,904,140	4,862,075
—	—	—	—	9,348	—	36,449
249	—	—	48	21,371	121,049	535,901
249	3,675	2,459	48	191,550	6,774,694	10,689,647
—	—	—	—	50,639	—	50,639
—	—	—	—	9,181	6,129	33,423
—	—	—	—	—	—	279,759
—	—	—	—	—	—	202,824
—	—	—	—	45	—	67,120
—	—	—	—	59,865	6,129	633,765
17,290	—	17,740	8,343	54,022	13,262	270,160
—	—	—	—	1,666	232	2,705
\$ 17,539	\$ 3,675	\$ 20,199	\$ 8,391	\$ 307,103	\$ 6,794,317	\$ 11,596,277

Interfund receivables and payables are the result of interfund loans that are not expected to be repaid within one year. The \$2.2 billion in nonmajor governmental funds payable from the General Fund is primarily the result of legislation authorizing the transfer of cash from special revenue funds to the General Fund. Table 36 presents the interfund receivables and payables.

Table 36**Schedule of Interfund Receivables and Payables**

June 30, 2005

(amounts in thousands)

Interfund Receivables	General Fund	Transportation Construction Fund	Nonmajor Governmental Funds	Water Resources Fund	Nonmajor Enterprise Funds	Fiduciary Funds	Total
Governmental funds							
General Fund	\$ —	\$ —	\$ 2,261,411	\$ —	\$ 7,100	\$ 1,011,800	\$ 3,280,311
Nonmajor governmental funds ..	13,849	628,900	—	—	—	—	642,749
Total governmental funds ..	13,849	628,900	2,261,411	—	7,100	1,011,800	3,923,060
Enterprise funds	829	—	—	—	2,300	—	3,129
Internal service funds	3,000	—	2,257	91,517	—	—	96,774
Fiduciary funds	134,301	—	—	—	—	—	134,301
Total primary government	\$ 151,979	\$ 628,900	\$ 2,263,668	\$ 91,517	\$ 9,400	\$ 1,011,800	\$ 4,157,264

Due from primary government and due to component units represent short-term receivables and payables between the primary government and component units resulting from the time lag between the dates that goods and services are provided and received and the dates that payments between entities are made. Table 37 presents the due from primary government and due to component units.

Table 37**Schedule of Due From Primary Government and Due To Component Units**

June 30, 2005

(amounts in thousands)

Due From	Due To			Total
	University of California	Public Employees' Benefits	Nonmajor Component Units	
Governmental funds				
General Fund	\$ 140,257	\$ 17	\$ —	\$ 140,274
Nonmajor governmental funds	30,322	—	—	30,322
Total governmental funds	170,579	17	—	170,596
Public Building Construction Fund	25,653	—	—	25,653
Internal service funds	—	3,610	1,174	4,784
Total primary government	\$ 196,232	\$ 3,627	\$ 1,174	\$ 201,033

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B. Interfund Transfers

As required by law, transfers move money collected by one fund to another fund that does the disbursing. The General Fund and certain other funds transfer money to support various programs accounted for in other funds. The largest transfers from the General Fund to the nonmajor governmental funds were \$1.3 billion for the support of trial courts and \$1.2 billion to the Local Revenue Fund to repay the Vehicle License Fee gap loan to local governments. The \$918 million transfer from the Federal Fund to the nonmajor governmental funds was for the administration of the unemployment programs. The largest transfers from the nonmajor governmental funds to the General Fund were \$140 million from the Traffic Congestion Relief Fund and \$86 million from the Workers' Compensation Administration Revolving Fund to support General Fund programs. Table 38 presents interfund transfers of the primary government.

Table 38**Schedule of Interfund Transfers**

June 30, 2005

(amounts in thousands)

Transferred From	Transferred To		
	General Fund	Transportation Construction Fund	Nonmajor Governmental Funds
Governmental funds			
General Fund	\$ —	\$ —	\$ 3,002,509
Federal Fund	—	—	917,849
Transportation Construction Fund	19,222	—	33,282
Nonmajor governmental funds	350,917	2,590	199,651
Total governmental funds	370,139	2,590	4,153,291
Enterprise funds			
Nonmajor enterprise funds	32,952	6,886	3,437
Total enterprise funds	32,952	6,886	3,437
Internal service funds	3,500	1,152	6,254
Total primary government	\$ 406,591	\$ 10,628	\$ 4,162,982

Transferred To				
Unemployment Programs Fund	Public Building Construction Fund	Nonmajor Enterprise Funds	Fiduciary Funds	Total
\$ —	\$ —	\$ 96	\$ 4,229	\$ 3,006,834
12,141	—	—	—	929,990
—	—	—	—	52,504
—	—	3,272	1,034	557,464
12,141	—	3,368	5,263	4,546,792
—	462	40	—	43,777
—	462	40	—	43,777
39	—	—	—	10,945
\$ 12,180	\$ 462	\$ 3,408	\$ 5,263	\$ 4,601,514

NOTE 18: FUND DEFICITS AND ENDOWMENTS**A. Fund Deficits**

Table 39 shows the funds that had deficits.

Table 39**Schedule of Fund Deficits**

June 30, 2005

(amounts in thousands)

	Governmental Funds	Internal Service Funds	Component Units
Higher Education Construction Fund	\$ 315,617	\$ —	\$ —
Other Capital Projects Funds	8,107	—	—
Architecture Revolving Fund	—	14,314	—
Water Resources Revolving Fund	—	3,414	—
Public Employees' Benefits Fund	—	—	518,624
California Consumer Power and Conservation Financing Authority Fund	—	—	4,259
Total	\$ 323,724	\$ 17,728	\$ 522,883

B. Discretely Presented Component Unit Endowments and Gifts

The University of California, a discretely presented component unit, administers certain restricted nonexpendable, restricted expendable, and unrestricted endowments that are included in the related net asset categories of the government-wide and fund financial statements. As of June 30, 2005, the total value of restricted and unrestricted endowments and gifts was \$7.9 billion and \$1.1 billion, respectively. The university's policy is to retain appreciation on investments with the endowment after an annual income distribution. Endowment income capitalized to endowment principal that is available to meet future funding needs upon approval by the board of regents amounted to \$1.4 billion at June 30, 2005. The portion of investment returns earned on endowments and distributed each year to support current operations is based on a rate approved by the board of regents.

The University of California Hastings College of the Law holds six restricted nonexpendable and restricted expendable endowments. The income from these endowments is allocated to the college and recorded as gifts. During the year ended June 30, 2005, the income generated from these endowments was \$145 million. The income from three of these endowments is to be distributed exclusively to the college's students, while the income from the remaining three is to be used for financial support of any University of California law student. As of June 30, 2005, the fair market value of these six endowments was \$5 million.

NOTE 19: RISK MANAGEMENT

The primary government has elected, with a few exceptions, to be self-insured against loss or liability. Generally, the exceptions are when a bond resolution or a contract requires the primary government to purchase commercial insurance for coverage against property loss or liability. There have been no significant reductions in insurance coverage from the prior year. In addition, there has been no insurance settlement in

the last three years that has exceeded insurance coverage. The primary government generally does not maintain reserves. Losses are covered by appropriations from each fund responsible for payment in the year in which the payment occurs. All claim payments are on a "pay as you go" basis, with workers' compensation benefits for self-insured agencies being initially paid by the State Compensation Insurance Fund. The potential amount of loss arising from risks other than workers' compensation benefits is not considered material in relation to the primary government's financial position.

The discounted liability for unpaid self-insured workers' compensation losses is estimated to be \$2.8 billion as of June 30, 2005. This estimate is based on actuarial reviews of the State's employee workers' compensation program and includes indemnity payments to claimants, as well as all other costs of providing workers' compensation benefits, such as medical care and rehabilitation. The estimate also includes the liability for unpaid services fees, industrial disability leave benefits, and incurred but not reported amounts. The estimated total liability of approximately \$3.9 billion is discounted to \$2.8 billion using a 4% interest rate. Of the total, \$341 million is a current liability, of which \$208 million is included in the General Fund, \$132 million in the special revenue funds, and \$1 million in the internal service funds. The remaining \$2.5 billion is reported as other noncurrent liabilities in the government-wide Statement of Net Assets.

The University of California, a discretely presented component unit, is self-insured for medical malpractice, workers' compensation, employee health care, and general liability claims. These risks are subject to various claim and aggregate limits, with excess liability coverage provided by an independent insurer. Liabilities are recorded when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. These losses include an estimate for claims that have been incurred but not reported. The estimated liabilities are based upon an independent actuarial determination of the anticipated future payments, discounted at rates ranging from 4.0% to 6.0%. The other discretely presented component units do not have significant liabilities related to self-insurance.

Changes in the self-insurance claims liability for the primary government and the University of California are shown in Table 40.

Table 40

Schedule of Changes in Self-Insurance Claims

Years Ended June 30

(amounts in thousands)

	Primary Government		University of California – Discretely Presented Component Unit	
	2005	2004	2005	2004
Unpaid claims, beginning	\$ 2,724,835	\$ 2,828,010	\$ 566,962	\$ 520,177
Incurring claims	455,108	298,978	250,264	289,247
Claim payments	(372,225)	(402,153)	(255,399)	(242,462)
Unpaid claims, ending	\$ 2,807,718	\$ 2,724,835	\$ 561,827	\$ 566,962

NOTE 20: NONMAJOR ENTERPRISE SEGMENT INFORMATION

A segment is an identifiable activity reported as or within an enterprise fund or another stand-alone entity for which debt is outstanding and a revenue stream has been pledged in support of that debt. In addition, to qualify as a segment, an activity must be subject to an external requirement to separately account for revenues, expenses, gains and losses, assets, and liabilities of the activity. All of the activities reported in the following condensed financial information meet these requirements.

Table 41 presents the Condensed Statement of Net Assets, the Condensed Statement of Revenues, Expenses, and Changes in Fund Net Assets, and the Condensed Statement of Cash Flows for nonmajor enterprise funds that meet the definition of a segment. The primary sources of revenues for these funds follow.

High Technology Education Fund: Rental payments on public buildings which are used for educational and research purposes related to specific fields of high technology.

State University Dormitory Building Maintenance and Equipment Fund: Charges to students for housing and parking, and student fees for campus unions.

State Water Pollution Control Revolving Fund: Interest charged on loans to communities for construction of water pollution control facilities and projects.

Housing Loan Fund: Interest payments from low interest, long-term farm and home mortgage loan contracts to eligible veterans living in California.

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Table 41**Nonmajor Enterprise Segments**

(amounts in thousands)

Condensed Statement of Net Assets June 30, 2005	State University	
	High Technology Education	Dormitory Building Maintenance and Equipment
Assets		
Due from other funds	\$ 400	\$ —
Due from other governments	—	—
Other current assets	31,366	743,219
Capital assets	—	1,610,128
Other noncurrent assets	433,819	14,520
Total assets	\$ 465,585	\$ 2,367,867
Liabilities		
Due to other funds	\$ —	\$ 27,834
Due to other governments	—	—
Other current liabilities	34,782	108,906
Noncurrent liabilities	304,192	1,683,858
Total liabilities	338,974	1,820,598
Net assets		
Investment in capital assets, net of related debt	—	318,818
Restricted	126,611	389,887
Unrestricted	—	(161,436)
Total net assets	126,611	547,269
Total liabilities and net assets	\$ 465,585	\$ 2,367,867

Condensed Statement of Revenues, Expenses, and Changes in Fund Net Assets

Year Ended June 30, 2005

Operating revenues	\$ 36,737	\$ 378,670
Depreciation expense	—	(65,842)
Other operating expenses	(33,690)	(354,878)
Operating income (loss)	3,047	(42,050)
Nonoperating revenues (expenses)	—	(11,634)
Capital contributions	—	—
Transfers in	96	—
Transfers out	(462)	(2,484)
Change in net assets	2,681	(56,168)
Total net assets, July 1, 2004	123,930	603,437 *
Total net assets, June 30, 2005	\$ 126,611	\$ 547,269

Condensed Statement of Cash Flows

Year Ended June 30, 2005

Net cash provided (used) by:

Operating activities	\$ 37,571	\$ (112,532)
Noncapital financing activities	(358)	(55,926)
Capital and related financing activities	(37,060)	289,855
Investing activities	—	—
Net increase (decrease)	153	121,397
Cash and pooled investments at July 1, 2004	50,839	577,832
Cash and pooled investments at June 30, 2005	\$ 50,992	\$ 699,229

* Restated

State Water Pollution Control	Housing Loan	Total
\$ 2,215	\$ 3,615	\$ 6,230
148,082	—	148,082
318,430	596,114	1,689,129
—	2,498	1,612,626
2,016,992	1,613,948	4,079,279
\$ 2,485,719	\$ 2,216,175	\$ 7,535,346
\$ 873	\$ 22	\$ 28,729
—	242	242
26,540	110,404	280,632
264,752	1,862,321	4,115,123
292,165	1,972,989	4,424,726
—	2,497	321,315
746,497	240,689	1,503,684
1,447,057	—	1,285,621
2,193,554	243,186	3,110,620
\$ 2,485,719	\$ 2,216,175	\$ 7,535,346
\$ 47,907	\$ 119,029	\$ 582,343
—	(901)	(66,743)
(4,082)	(140,977)	(533,627)
43,825	(22,849)	(18,027)
(3,245)	1,827	(13,052)
73,182	—	73,182
—	—	96
—	—	(2,946)
113,762	(21,022)	39,253
2,079,792	264,208	3,071,367
\$ 2,193,554	\$ 243,186	\$ 3,110,620
\$ (56,553)	\$ 29,952	\$ (101,562)
38,618	(125,223)	(142,889)
—	—	252,795
6,296	46,259	52,555
(11,639)	(49,012)	60,899
329,962	610,145	1,568,778
\$ 318,323	\$ 561,133	\$ 1,629,677

NOTE 21: NO COMMITMENT DEBT

Certain debt of the nonmajor component units is issued to finance activities such as construction of new facilities and remodeling of existing facilities, as well as acquisition of equipment. This debt is secured solely by the credit of private and public entities and is administered by trustees independent of the State. As of June 30, 2005, these component units had \$17.2 billion of debt outstanding, which is not debt of the State.

The State has also entered into transactions that involve debt issued by four special purpose trusts that were created by one of its nonmajor component units, the California Infrastructure and Economic Development Bank. The special purpose trusts are legally separate entities that issued long-term debt for the primary purpose of financing certain costs of assets and obligations that are recoverable by utilities through electric rate charges. These costs may prevent the utilities from offering electricity at lower rates in a competitive market. As of June 30, 2005, the special purpose trusts had approximately \$1.5 billion of debt outstanding. Like the debt of nonmajor component units, the debt of the special purpose trusts is not debt of the State.

NOTE 22: CONTINGENT LIABILITIES

A. Litigation

The primary government is a party to numerous legal proceedings, many of which normally occur in governmental operations. To the extent they existed, the following were accrued as a liability in the government-wide financial statements: legal proceedings that were decided against the primary government before June 30, 2005; legal proceedings that were in progress as of June 30, 2005, and were settled or decided against the primary government as of February 28, 2006; and legal proceedings having a high probability of resulting in a decision against the primary government as of February 28, 2006, and for which amounts could be estimated. In the governmental fund financial statements, the portion of the liability that is expected to be paid within the next 12 months is recorded as a liability of the fund from which payment will be made. In the proprietary fund financial statements, the entire liability is recorded in the fund from which payment will be made.

In addition, the primary government is involved in certain other legal proceedings that, if decided against the primary government, may impair its revenue sources or require it to make significant expenditures. Because of the prospective nature of these proceedings, no provision for the potential liability has been made in the financial statements.

Following are the more significant lawsuits pending against the primary government.

The primary government was a defendant in *County of San Diego v. Commission on State Mandates et al.*, regarding certain unreimbursed costs for the care of medically indigent adults (MIAs). In 1997, the California Supreme Court ruled that, by excluding MIAs from Medi-Cal, the State had mandated a new program on the counties. San Diego County prevailed, and the State paid the County \$3 million for unreimbursed costs related to the mandated services. The commission has taken the position that it would be bound to apply the holding of the San Diego County case to any new claim for prospective relief brought by any county as a "test claim." A test claim filed by the County of San Bernardino (county) regarding certain unreimbursed costs for the care of MIAs is now pending before the commission. In recent years, counties have collectively received approximately \$1.0 billion annually in vehicle license fee revenue and \$410 million annually in sales tax revenue to fund various public health programs, which include programs that provide services to MIAs;

however, the county claims that funding is inadequate to cover all services to MIAs mandated by the State. The county's test claim poses a potential for a negative impact on the General Fund in the amount of the unreimbursed costs for all similarly situated county claimants for a period of years, as determined by the commission. The amount demanded by the county for the 2000-01 fiscal year alone is over \$9 million. Certain estimates of the annual cost of services rendered by all counties to MIAs exceed \$4.0 billion. It is difficult to determine how much could be recovered by the counties, because each situation is fact-driven and lack of documentation was a major concern in the San Diego case.

The primary government is a party in several lawsuits which allege that the gross receipts from the plaintiffs' sale of certain short-term financial instruments constitute business income and therefore must be included in the denominator of the California sales factor of the apportionment formula to be applied to the business income of the plaintiffs. The plaintiffs further contend that the exclusion is a violation of their rights under the due process and commerce clauses of the U.S. Constitution. The Franchise Tax Board (board) maintains that, under pertinent tax statutes, the return of the original loan proceeds from a maturing debt instrument is not a "gross receipt" for sales factor purposes and thus must be excluded from the denominator of the sales factor. The board estimates that the amount at issue to all taxpayers for prior years could exceed \$500 million. The lead case in this issue is currently waiting the California Supreme Court to set the case for oral argument. The other five cases are on hold and are pending the lead case decision. In addition, one taxpayer is claiming that the board improperly excluded value-added taxes from the denominator of the sales factor and should have valued property for purposes of the property factor of the apportionment formula at current fair market value rather than historical cost.

The primary government is a defendant in class action lawsuit alleging the State's repeal of the Vehicle License Fee offset triggered a cost of living adjustment increase for all CalWORKs' beneficiaries pursuant to Welfare and Institutions Code section 11453(c)(3). The superior court entered judgment for the petitioners. The case on appeal has been fully briefed and the parties are awaiting notification of the date for oral arguments. The Department of Social Services estimates that the amount at issue could exceed \$330 million, plus interest, for amounts related to fiscal years 2003-04, 2004-05, and 2005-06.

The primary government is a defendant in a lawsuit alleging the petitioners, Medi-Cal beneficiaries, seek direct reimbursement from the Department of Health Services for covered expenses they paid out-of-pocket while petitioners applications for benefits were pending. The Department may be liable for more than \$800 million in out-of-pocket payments. The Department is working with petitioners' counsel to address the directive of the First District Court of Appeal as to the creation of an acceptable implementation plan and notice to beneficiaries regarding reimbursement procedures for the out-of-pocket payments. A hearing on the proposed plan is set for January 2006.

The primary government was a defendant in an action, *Sanchez, et al., v. Johnson, et al.*, where a class of persons with developmental disabilities is seeking injunctive relief against the Health and Human Services Agency and the departments of Developmental Services, Mental Health, and Finance, to obtain higher funding rates for service providers. The State received favorable rulings from the Ninth District Court of Appeals. The Plaintiff has declined to seek review by the U.S. Supreme Court.

The primary government is a party to the lawsuit of *Alan J. Titus and Marjorie Goldman v. County of Marin*, an action related to property taxation. Propositions 13 and 8 limit property tax to 1% of a property's base year value, which is essentially the acquisition value. This base year value can be increased by not more than 2% per annum but may be reduced by any amount to reflect loss of value. The plaintiffs contend that the common assessor practice whereby value is brought back up after a temporary reduction without regard to the 2% limitation is unconstitutional. The trial court ruled against taxpayers Titus and Goldman, who appealed. The State received favorable rulings through the U.S. Supreme Court, which denied plaintiffs petition for review.

The University of California (UC), the State Compensation Insurance Fund (SCIF), the California Housing Finance Agency (CalHFA), and nonmajor discretely presented component units are contingently liable in connection with claims and contracts, including those currently in litigation, arising in the normal course of their activities. Although there are inherent uncertainties in any litigation, the management and the general counsel of UC, SCIF, and CalHFA are of the opinion that the outcome of such matters either is not expected to have a material effect on the financial statements or cannot be estimated at this time.

B. Federal Audit Exceptions

The primary government receives substantial funding from the federal government in the form of grants and other federal assistance. The primary government, UC, and CalHFA are entitled to these resources only if they comply with the terms and conditions of the grants and contracts and with the applicable federal laws and regulations; they may spend these resources only for eligible purposes. If audits disclose exceptions, the primary government, UC, and CalHFA may incur a liability to the federal government.

NOTE 23: PENSION TRUSTS

Three retirement systems, the California Public Employees' Retirement System (CalPERS), the California State Teachers' Retirement System (CalSTRS), and the University of California Retirement System, all of which are fiduciary component units, are included in the pension and other employee benefit trust funds column of the fiduciary funds and similar component units' financial statements. The pension liability for all pension and other employee benefit trust funds was determined in accordance with GASB Statement No. 27, *Accounting for Pensions by State and Local Government Employers*. The amounts of the pension liability for all pension and other employee benefit trust funds are presented in Table 43 as the net pension obligation (NPO) as of June 30, 2005. The investments of these fiduciary component units are included in the primary government investments presented in Table 2 in Note 3, Deposits and Investments.

CalPERS administers five defined benefit retirement plans: the Public Employees' Retirement Fund (PERF), the Judges' Retirement Fund (JRF), the Judges' Retirement Fund II (JRF II), the Legislators' Retirement Fund (LRF), and the Volunteer Firefighters' Length of Service Award Fund (VFF). CalPERS also administers three defined contribution plans: the State Peace Officers' and Firefighters' Defined Contribution Plan Fund (SPOFF), the public employee Replacement Benefit Fund (RBF), and the public employee Supplemental Contributions Program Fund (SCPF). CalPERS issues a publicly available financial report that includes financial statements and required supplementary information for these plans. This report may be obtained by writing to the California Public Employees' Retirement System, Fiscal Services Division, P.O. Box 942703, Sacramento, California 94229 or by visiting the CalPERS website at www.CalPERS.ca.gov.

CalPERS uses the accrual basis of accounting. Member contributions are recognized when due. The VFF, the SPOFF, and the RBF are funded only by employer contributions that are recorded when due, and the employer has made a formal commitment to provide the contributions. Benefits under the defined benefit plans and refunds are recognized when due, in accordance with the terms of each plan.

CalSTRS administers three defined benefit retirement plans within the State Teachers' Retirement Plan: the Defined Benefit Program (DB Program), the Defined Benefit Supplement Program, and the Cash Balance Benefit Program. CalSTRS also offers, through a third-party administrator, a defined contribution plan that meets the requirements of Internal Revenue Code Section 403(b). The Teachers' Health Benefits Fund provides post-employment health benefits to retired members of the DB Program. CalSTRS issues a publicly available financial report that includes financial statements and required supplementary information for these

plans. This report may be obtained from the California State Teachers' Retirement System, P.O. Box 15275, Sacramento, California 95851.

CalSTRS uses the accrual basis of accounting. Member contributions are recognized in the period in which the contributions are due. Employer and primary government contributions are recognized when due, and the employer or the primary government has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable, in accordance with the retirement and benefits programs.

A. Public Employees' Retirement Fund

1. Fund Information

Plan Description: CalPERS administers the PERF, which is an agent multiple-employer defined benefit retirement plan. Employers participating in the PERF include the primary government and certain discretely presented component units, 61 school employers, and 1,462 public agencies as of June 30, 2005. For reporting purposes, the financial information of the RBF is combined with that of the PERF.

The amount by which the actuarial accrued liability exceeded the actuarial value of assets in the PERF for the primary government and other participating agencies was \$24.7 billion at June 30, 2004. This is a result of the difference between the actuarial value of assets of \$169.9 billion and the actuarial accrued liability of \$194.6 billion. Contributions are actuarially determined.

2. Employer's Information

Plan Description: The primary government and certain discretely presented component units contribute to the PERF. CalPERS acts as a common investment and administrative agent of the primary government and the other member agencies. The discretely presented component units' participation in the PERF is not a material portion of the program. The primary government employees served by the PERF include: first-tier and second-tier miscellaneous and industrial, California Highway Patrol, peace officers and firefighters, and other safety members. The payroll for primary government employees covered by the PERF in the year ended June 30, 2005, was approximately \$12.9 billion.

All employees in a covered class of employment who work half-time or more are eligible to participate in the PERF. The PERF provides benefits based on members' years of service, age, final compensation, and benefit

formula. Vesting occurs after five years, or after ten years for second-tier employees. The PERF provides death, disability, and survivor benefits. The benefit provisions are established by statute.

Funding Policy: Benefits are funded by contributions from members and the primary government and earnings from investments. Member and primary government contributions are a percentage of applicable member compensation. Member rates are defined by law and based on the primary government's benefit formula. The primary government contribution rates are determined by periodic actuarial valuations.

Employees, with the exception of employees in the second-tier plans, contribute to the fund based on the required contribution rates. The contribution rates of active plan members are based on a percentage of salary over a monthly base compensation amount of \$133 to \$863. Employees' required contributions vary from 5.0% to 8.0% of their salary over the base compensation amount.

All of the primary government employees served by the PERF are now covered by group term life insurance. The required employer contribution rates for the primary government are shown in Table 42.

Table 42**Schedule of Required Employer Contribution Rates for the Primary Government by Member Category**

Year Ended June 30, 2005

	Normal Cost	Unfunded Liability	Group Term Life Benefit	Total Rate
Miscellaneous members				
First tier	9.928 %	6.982 %	0.112 %	17.022 %
Second tier	6.122	6.982	0.112	13.216
Industrial (first and second tier).....	12.765	3.530	0.091	16.386
California Highway Patrol	15.307	18.127	0.000	33.434
Peace officers and firefighters	17.276	6.487	0.078	23.841
Other safety members	15.028	5.607	0.138	20.773

For the year ended June 30, 2005, the annual pension cost (APC) and the amount of contributions made by the primary government were each \$2.5 billion. The APC and the percentage of APC contributed for the last three years are shown in Table 43. Actuarial valuations of the PERF are performed annually. Information from the last valuation, which was performed as of June 30, 2004, is also shown in Table 43 for the primary government.

B. Judges' Retirement Fund

Plan Description: CalPERS administers the JRF, which is an agent multiple-employer defined benefit retirement plan. The JRF membership includes justices of the Supreme Court and courts of appeal, as well as judges of superior courts, appointed or elected prior to November 9, 1994. There are 59 employers participating in the JRF for the year ended June 30, 2005. The payroll for employees covered by the JRF for the year ended June 30, 2005, was approximately \$134 million. The primary government pays the employer contributions for all employees covered by the JRF.

The JRF provides benefits based on a member's years of service, age, final compensation, and benefit formula. Vesting occurs after five years. The JRF provides death, disability, and survivor benefits. Benefits for the JRF are established by the Judges' Retirement Law.

Funding Policy: The contribution rate of active plan members is defined by law and is based on a percentage of salary over a base compensation amount. For the year ended June 30, 2005, the required member rate for the JRF was 8.0%.

The contributions of the primary government to the JRF are not actuarially determined. Contributions are determined by state statute. As of June 30, 2005, employer contributions are required to be 8.0% of applicable member compensation. Other funding to meet benefit payment requirements of the JRF is currently provided by: filing fees, which require varying amounts, depending on fee rate and number of filings; investments, which earn the current yield on short-term investments; and the primary government's balancing contributions, as required by the Judges' Retirement Law. The balancing contributions are an amount at least equal to the

estimated benefits payable during the ensuing fiscal year, less the sum of the estimated member contributions during the ensuing fiscal year and net assets available for benefits at the beginning of the fiscal year ("pay as you go" basis).

The annual pension cost (APC) and the amount of employer contributions made to the JRF for the year ended June 30, 2005, were \$184 million and \$127 million, respectively. The net pension obligation (NPO) of the JRF at June 30, 2005, was \$1.13 billion, an increase of \$57 million over last year's balance of \$1.07 billion. The APC is comprised of \$190 million for the annual required contribution (ARC), \$75 million for interest on the NPO, and \$81 million for the adjustment to the ARC. An actuarial valuation of the JRF's assets and liabilities is made annually. The APC, the percentage of APC contributed, and the NPO for the last three years are shown in Table 43. Information on the last valuation, which was performed as of June 30, 2004, is shown in Table 43. The aggregate cost method that was used for the June 30, 2004, valuation does not identify or separately amortize the unfunded actuarial accrued liability; therefore, this liability is not shown in Table 43.

C. Judges' Retirement Fund II

Plan Description: CalPERS administers the JRF II, which is an agent multiple-employer defined benefit retirement plan. The membership of the JRF II includes justices of the same courts covered by the JRF who were appointed or elected on or subsequent to November 9, 1994. There are 59 employers participating in the JRF II. The payroll for employees covered by the JRF II for the year ended June 30, 2005, was approximately \$105 million. The primary government pays the employer contributions for all employees covered by the JRF II.

The JRF II provides benefits based on a member's years of service, age, final compensation, and benefit formula. Vesting occurs after five years. The JRF II provides death, disability, and survivor benefits. Benefits for the JRF II are established by the Judges' Retirement System II Law.

Funding Policy: The required contribution rate of active plan members is defined by law and is based on a percentage of salary over a base compensation amount. For the year ended June 30, 2005, the required member rate for the JRF II was 8.0%, and the primary government's contribution rate for the JRF II was 20.25% of applicable member compensation.

Actuarial valuations for the JRF II are required to be carried out annually. The legislated primary government contribution rate is adjusted periodically as part of the annual Budget Act, in order to maintain or restore the actuarial soundness of the fund.

For the year ended June 30, 2005, the annual pension cost (APC) and the amount of contributions made for the JRF II were approximately \$21 million. The APC and the percentage of APC contributed for the year ended June 30, 2005, are shown in Table 43. Information on the last valuation, which was performed as of June 30, 2004, is also shown in Table 43.

D. Legislators' Retirement Fund

Plan Description: CalPERS administers the LRF, which is a single-employer defined benefit retirement plan. The eligible membership of the LRF includes state legislators serving in the legislature prior to November 1, 1990, constitutional officers, and legislative statutory officers. The payroll for the employees covered by the LRF for the year ended June 30, 2005, was approximately \$1.7 million.

The LRF provides benefits based on a member's years of service, age, final compensation, and benefit formula. Vesting occurs after five years. The plan provides death, disability, and survivor benefits. Benefits for the LRF are established by the Legislators' Retirement Law.

The LRF is currently in transition. The number of legislators eligible to participate in the LRF is declining as incumbent legislators leave office and are replaced by new legislators who are not eligible to participate in the program. Eventually, the only active members in the LRF will be approximately 16 constitutional officers (including the Insurance Commissioner and members of the Board of Equalization) and approximately 4 legislative statutory officers.

Funding Policy: The employer contribution requirements of the LRF are based on actuarially determined rates. An actuarial valuation of the LRF's assets and liabilities is required at least every two years. Member contribution rates are defined by law. For the year ended June 30, 2005, contributions made by employees were not required because the plan was superfunded. By definition, "superfunded" is when the plan's actuarial value of assets exceeds the present value of future benefits for current members. However, some members made contributions towards military service and prior service.

The net pension obligation (NPO) of the LRF on June 30, 2005, was approximately \$10 million. There was no annual pension cost (APC) because the annual required contribution (ARC) equaled zero and the interest on the NPO closely approximated the adjustment to the ARC. The APC, the percentage of APC contributed, and the NPO for the last three years are shown in Table 43. An actuarial valuation of the LRF's assets and liabilities is made annually. Information on the last valuation, which was performed as of June 30, 2004, is also shown in Table 43. The aggregate cost method that was used for the June 30, 2004, valuation does not identify or separately amortize the unfunded actuarial accrued liability; therefore, this liability is not shown in Table 43.

E. Volunteer Firefighters' Length of Service Award Fund

Plan Description: CalPERS administers the VFF, which is an agent multiple-employer defined benefit retirement plan. The VFF membership includes volunteer firefighters. There were 61 fire departments participating in the VFF for the year ended June 30, 2005.

The actuarial accrued liability of the VFF exceeded the actuarial value of assets by \$550,000 at June 30, 2004. This is a result of the difference between the actuarial accrued liability of \$3.5 million and the actuarial value of assets of \$3.0 million. Contributions are actuarially determined.

F. State Peace Officers' and Firefighters' Defined Contribution Plan Fund

Plan Description: CalPERS administers the SPOFF, which is a defined contribution pension plan. The plan is a qualified money purchase pension plan under Section 401(a) of Title 26 of the Internal Revenue Code, and it is intended to supplement the retirement benefits provided by the Public Employees' Retirement Fund to eligible correctional employees employed by the State of California.

Funding Policy: Contributions to the plan are funded entirely by the primary government with a contribution rate of 2% of the employee's base pay, not to exceed contribution limits established by the Internal Revenue Code. Contribution requirements are established and may be amended through a memorandum of understanding from the State of California Department of Personnel Administration. These contributions, as well as the participant's share of the net earnings of the fund, are credited to the participant's account. For the

year ended June 30, 2005, contributions by the primary government to the SPOFF were approximately \$41.4 million.

The net earnings of the fund are allocated to the participant's account as of each valuation date, in the ratio that the participant's account balance bears to the aggregate of all participants' account balances. The benefit paid to a participant will depend only on the amount contributed to the participant's account and earnings on the value of the participant's account. Plan provisions are established by and may be amended by statute. At June 30, 2005, there were 34,922 participants.

G. Teachers' Retirement Fund

Plan Description: CalSTRS administers the Teachers' Retirement Fund, which is an employee benefit trust fund created to administer the State Teachers' Retirement Plan (STRP). The STRP is a defined benefit pension plan that provides for retirement, disability, and survivor benefits. The STRP is comprised of three programs: the Defined Benefit (DB) Program, the Defined Benefit Supplement (DBS) Program, and the Cash Balance (CB) Benefit Program. The STRP is a cost-sharing, multiple-employer, defined benefit retirement plan that provides pension benefits to teachers and certain other employees of the California public school system.

Membership in the DB Program is mandatory for all employees meeting the eligibility requirements. The DB Program provides benefits based on a member's age, final compensation, and years of service. Vesting occurs after five years. In addition, the retirement program provides benefits to members upon disability and to survivors upon the death of eligible members. The Teachers' Retirement Law establishes the benefits for the DB Program. At June 30, 2005, the DB Program had approximately 1,300 contributing employers and as of June 30, 2004, had approximately 561,000 active and inactive program members, and 193,000 benefit recipients. The primary government is a nonemployer contributor to the DB Program. The payroll for employees covered by the DB Program for the year ended June 30, 2005, was approximately \$23.9 billion.

Membership in the DBS Program is automatic for all members of the DB Program. The DBS Program provides benefits based on the balance of member accounts. Vesting occurs immediately. The Teachers' Retirement Law establishes the benefits for the DBS Program. The primary government does not contribute to the DBS Program.

The CB Program is designed for employees of California public schools who are hired to perform creditable service for less than 50% of the full-time equivalent for the position. Participation in the CB Program is optional to employers. However, if the employer elects to offer the CB Program, each eligible employee will automatically be covered by the CB Program unless the member elects to participate in the DB Program or an

alternative plan provided by the employer within 60 days of hire. At June 30, 2005, the CB Program had 28 contributing school districts and approximately 21,000 contributing participants.

Funding Policy: DB Program benefits are funded by contributions from members, employers, the primary government, and earnings from investments. Member and employer contributions are a percentage of applicable member earnings. The Teachers' Retirement Law governs member rates, employer contribution rates, and primary government contributions.

The DB Program contribution rate of members is 6% of creditable compensation through December 31, 2010, increasing to 8% thereafter for service less than or equal to one year of creditable service per fiscal year. The employer contribution rate is 8.25% of creditable compensation for service less than or equal to one year of creditable service per fiscal year; for service in excess of one year within one fiscal year, the employer

contribution rate is 0.25%. In fiscal year 2004-05, the General Fund contribution was 2.017% of total creditable compensation of the fiscal year ending in the prior calendar year. Education code 22955(b) states that the General Fund will contribute additional quarterly payments at a contribution rate of 0.524% of creditable earnings of the fiscal year ending in the immediately preceding calendar year when there is an unfunded obligation or a normal cost deficit. The percentage is adjusted up to 0.25% per year to reflect the contributions required to fund the unfunded obligation or the normal cost deficit. However, the transfer may not exceed 1.505% of creditable compensation from the immediately preceding calendar year. The normal cost deficit is the difference between the normal cost rate and the member and employer contributions, which equal 16.00% of creditable compensation. Based on the most recent actuarial valuation, as of June 30, 2004, there is no normal cost deficit or an unfunded obligation for benefits in place as of July 1, 1990. Therefore, the General Fund is not required to contribute quarterly payments starting October 1, 2005, at a contribution rate of 0.524%.

The DBS Program member contribution rate is 2% of creditable compensation for service less than or equal to one year of creditable service per fiscal year. For service in excess of one year within one fiscal year, the member contribution rate is 8% and the employer rate is 8%.

For the year ended June 30, 2005, the annual pension cost (APC) for the DB Program was approximately \$3.8 billion, and the employer and primary government contributions were approximately \$2.0 billion and \$0.6 billion, respectively. The APC and the percentage of APC contributed for the last three years are shown in Table 43. Actuarial valuations of the DB Program are performed biennially. Information from the last valuation is shown in Table 43.

H. CalSTRS Voluntary Investment Program

Plan Description: CalSTRS administers the Voluntary Investment Program (VIP), a 403(b) program, through a third-party administrator. The VIP is a defined contribution plan and is open to any employee who is eligible to participate. Contributions to the program are voluntary; however, the Internal Revenue Code does impose a maximum amount that can be contributed annually. At June 30, 2005, the VIP had 403 participating employers (school districts) and 3,519 plan members.

I. Teachers' Health Benefits Fund

Plan Description: CalSTRS administers the Teachers' Health Benefits Fund (THBF), which was established pursuant to Chapter 1032, Statutes of 2000 (SB 1435), to provide the Medicare Premium Payment Program for eligible retired members of the DB Program. At June 30, 2005, there were 6,004 benefit recipients.

Funding Policy: The THBF is funded as needed from the monthly DB Program statutory employer contribution that exceeds the amount needed to finance the liabilities of the DB Program based on the June 30, 2000 actuarial valuation of the DB Program.

J. University of California Retirement System

The University of California Retirement System (UCRS) consists of: the University of California Retirement Plan (UCRP), a single-employer defined benefit plan funded with university and employee contributions; the Public Employees' Retirement System Voluntary Early Retirement Incentive Program (PERS-VERIP), a defined benefit plan for university employees who elected early retirement under the plan; and the University of California Retirement Savings Program that includes three defined contribution plans with options to

participate in internally and externally managed investment portfolios funded with employee non-elective and elective contributions. Most university career employees participate in the UCRS.

The UCRS uses the accrual basis of accounting. As of June 30, 2005, employee and employer contributions were not required to UCRP and PERS-VERIP, due to the fully funded status of each plan. Any contributions made in connection with service credit buybacks are recognized in the period in which they are made. Benefits and refunds are recognized when due and payable, in accordance with the terms of each plan.

The UCRP provides lifetime retirement income, disability protection, death benefits, and pre-retirement survivor benefits to eligible employees of the University of California and its affiliates. Membership in the retirement plan is required for all employees appointed to work at least 50% time for a year or more. Generally, an employee must have five years of service to be entitled to plan benefits. The maximum monthly benefit is 100% of the employee's highest average compensation over a 36-month period. The amount of the pension benefit is determined by salary rate, age, and years of service credit, with certain cost-of-living adjustments.

Members' contributions to the UCRP are accounted for separately and accrue interest at 6% annually. Upon termination, members can elect a refund of their contributions plus accumulated interest. Vested terminated members who are eligible to retire can also elect a lump-sum payment equal to the present value of their accrued benefits. Either action results in the member's forfeiture of rights to further accrued benefits.

At June 30, 2005, plan membership totaled 188,790, comprised of 124,642 active members, 22,671 inactive members (terminated vested employees entitled to benefits but not yet receiving them), and 41,477 retirees and beneficiaries currently receiving benefits. The active members include 71,367 current employees who are fully vested and 53,275 nonvested current employees covered by the plan. A total of 24,452 terminated nonvested employees are not members of the plan but are eligible for a refund.

The funding policy of the Regents of the University of California (regents) provides for actuarially determined contributions at rates that provide for sufficient assets to be available when benefits are due. The contribution rate is determined using the entry age normal actuarial funding method. The significant actuarial assumptions used to compute the actuarially determined contribution are the same as those used to compute the actuarial accrued liability.

The annually determined rates for employer contributions as a percentage of payroll are based on recommendations of the consulting actuary and on appropriations received from the primary government.

Employees may be required to contribute to the UCRP. The rate of employee contributions is established annually as a percentage of covered wages, pursuant to the regents' funding policy, recommended and certified by an enrolled, independent actuary and approved by the regents, the plan's trustee. During the year ended June 30, 2005, employee contributions to the UCRP were redirected to the University of California Defined Contribution Plan.

For the year ended June 30, 2005, there were no employer contributions, annual pension costs, or net pension obligations. The annual pension cost was equal to the actuarially determined contribution.

The actuarial value of assets was determined using techniques that smooth the effect of short-term volatility in the fair value of investments over a five-year period. The actuarial value of assets in excess of the actuarial accrued liability is being amortized as a level percentage of projected payroll on an open basis. The remaining amortization period at June 30, 2005, was three years.

The PERS-VERIP is a defined benefit pension plan providing lifetime supplemental retirement income and survivor benefits to members of the University of California CalPERS program (UC-PERS) who elected early retirement under provisions of the plan. The university contributed to the CalPERS program on behalf of these UC-PERS members. At June 30, 2005, there were 785 retirees or beneficiaries receiving benefits under this voluntary early retirement program. The cost of contributions made to the plan is borne entirely by the university and the U.S. Department of Energy laboratories. Over the five-year period ended June 30, 1996, the university and the U.S. Department of Energy laboratories were required to make contributions to the plan sufficient to maintain the promised benefits and the qualified status of the plan, as determined by the plan's consulting actuary.

The University of California Retirement Savings Program includes three defined contribution plans (Defined Contribution Plan, Tax Deferred 403(b) Plan, and Tax Deferred 457(b) Plan) providing savings incentives and additional retirement security that are generally available to all University employees. Participants' interests in the plans are fully and immediately vested and are distributable at death, retirement or termination of employment. Participants may also elect to defer distribution of the account until age 70 1/2 or separation from service after age 70 1/2, whichever is later, in accordance with Internal Revenue Code minimum distribution requirements. The Plans also accept pretax rollover contributions from other 401(a), 401(k), 403(b) and governmental 457(b) Plans.

The Defined Contribution Plan (the DC Plan) accepts both after-tax and pretax contributions. Pretax contributions are fully vested and are mandatory for all employees who are members of the UCRP. Monthly employee contributions range from approximately 2% to 4% of covered wages depending upon whether wages are below or above the Social Security wage base. The university has a provision for matching employer and employee contributions to the DC Plan for certain summer session teaching or research compensation for eligible academic employees. Employer contributions to the DC Plan were \$3.5 million for the year ended June 30, 2005.

The university's Tax Deferred 403(b) Plan (the 403(b) Plan) accepts pretax contributions. In October 2004, the university established a Tax Deferred 457(b) Plan (the 457(b) Plan) to accept pretax contributions. There are no employer contributions to the 403(b) Plan and the 457(b) Plan.

Participants in the DC Plan and the 403(b) Plan may direct their elective and nonelective contributions to investment funds managed by the treasurer of the regents. Participants may also invest contributions in, and transfer plan accumulations to, certain external mutual funds on a custodial plan basis. The participants' interest in external mutual funds is shown separately on the statement of the plans' fiduciary net assets. Participants in the 457(b) Plan may direct their elective contributions only to investment funds managed by the treasurer.

Additional information on the retirement plans can be obtained from the 2004-05 annual reports of the UCRP, the PERS-VERIP, the University of California Retirement Savings Plans. These reports may be obtained from the University of California, Office of the President – HR/Benefits Dept., Financial Services and Plan Disbursements, 300 Lakeside Drive, Suite 400, Oakland, California 94612.

The annual required contribution for the current year was determined as part of the June 30, 2005, actuarial valuation, which is the latest available information, using the entry age normal actuarial cost method. Significant actuarial assumptions used in the valuation are shown in Table 43. Information from the last valuation is also shown in Table 43.

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Table 43**Actuarial Information – Pension Trusts – Primary Government**

June 30, 2005

	Public Employees' Retirement Fund	Judges' Retirement Fund	Judges' Retirement II Fund
Last actuarial valuation	June 30, 2004	June 30, 2004	June 30, 2004
Actuarial cost method	Individual Entry Age Normal	Aggregate Cost	Aggregate Entry Age Normal
Amortization method	Level % of Payroll, Closed	None	Level % of Payroll, Closed
Remaining amortization period	22 to 30 years	None	Average of 30 Years
Asset valuation method	Smoothed Market Value	Market Value	Smoothed Market Value
Actuarial assumption			
Investment rate of return	7.75 %	7.00 %	7.25 %
Projected salary increase	3.25 - 19.95	3.25	3.25
Includes inflation at	3.00	3.00	3.00
Post-retirement benefit increases	2 - 5	3.25	3.00
Annual pension costs (in millions)			
Year ended 6/30/03	\$ 1,172	\$ 186	\$ 15.9
Year ended 6/30/04	2,121	191	18.6
Year ended 6/30/05	2,480	184	21.2
Percent contribution			
Year ended 6/30/03	100 %	53 %	96 %
Year ended 6/30/04	100	57	102
Year ended 6/30/05	100	69	100
Net pension obligation (in millions)			
Year ended 6/30/03	—	\$ 987	—
Year ended 6/30/04	—	1,069	—
Year ended 6/30/05	—	1,127	—
Funding as of last valuation (in millions)			
Actuarial value – assets	\$ 67,081	N/A	\$ 129.2
Actuarial accrued liabilities (AAL) – entry age	79,800	N/A	137.7
Excess of actuarial value of assets over AAL (EAV) (unfunded actuarial accrued liability (UAAL))	(12,719)	N/A	(8.5)
Covered payroll	12,624	N/A	99
Funded ratio	84.1 %	N/A	93.8 %
EAV (UAAL) as percent of covered payroll	100.8 %	N/A	8.6 %

* The State is a non-employer contributor to the State Teacher's Retirement Defined Benefit Program Fund, a cost-sharing multiple-employer plan. The annual Pension cost includes the amount related to both the State and the local government employers. The notion of ARC and NPO does not apply to cost-sharing employer plans. According to the provisions of the Education Code, the State and local government employers contributed \$595 million and \$2.0 billion, respectively, for the year ending June 30, 2005. Based on the most recent actuarial valuation dated June 30, 2004, current statutory contributions are sufficient to fund normal costs but are not expected to be sufficient to amortize the unfunded actuarial obligation. However, future estimates of the actuarial unfunded obligation may change due to market performance, legislative actions and other experience that may differ from the actuarial assumptions.

Legislators' Retirement Fund	State Teachers' Retirement Defined Benefit Program Fund *	University of California Retirement Plan Fund	Voluntary Early Retirement Incentive Plan Fund
June 30, 2004	June 30, 2004	June 30, 2005	June 30, 2005
Aggregate Cost	Entry Age Normal	Entry Age Normal	Unit Credit
None	Level % of Payroll, Open	Level % of Payroll, Open	N/A
None	Not amortizable	3 Years	N/A
Smoothed Market Value	Expected Value, With 33% Adjustment to Market Value	Smoothed Fair Value	Fair Value
7.00 %	8.00 %	7.50 %	7.50 %
3.25	4.25	4.5 - 6.5	N/A
3.00	3.25	4.00	4.00
3.00	2.00	N/A	N/A
\$ —	\$ 2,545	—	—
—	3,539	—	—
—	3,836	—	—
— %	91 %	N/A	N/A
—	67	N/A	N/A
—	68	N/A	N/A
\$ 10	—	—	—
10	—	—	—
10	—	—	—
N/A	\$ 114,094	\$ 41,085	\$ 77.8
N/A	138,254	37,252	45.8
N/A	(24,160)	3,833	32.0
N/A	23,764	8,150	—
N/A	82.5 %	110.3 %	169.8 %
N/A	101.7 %	47.0 %	—

NOTE 24: POST-RETIREMENT HEALTH CARE BENEFITS

Health care and dental benefits are provided by the primary government and certain discretely presented component units, to annuitants of retirement systems to which the primary government contributes as an employer. The discretely presented component units' participation in these plans is not a material portion of the program. To be eligible for these benefits, first-tier plan annuitants must retire on or after age 50 with at least five years of service, and second-tier plan annuitants must retire on or after attaining age 55 with at least 10 years of service. In addition, annuitants must retire within 120 days of separation from employment to be eligible to receive these benefits. As of June 30, 2005, approximately 124,700 annuitants were enrolled to receive health benefits and approximately 101,700 annuitants were enrolled to receive dental benefits. In accordance with the California Government Code, the primary government generally pays 100% of the health insurance cost for annuitants, plus 90% of the additional premium required for the enrollment of family members of annuitants. Although the California Government Code does not specify the primary government's contribution toward dental insurance costs, the primary government generally pays all or a portion of the dental insurance cost for annuitants, depending upon the completed years of credited state service at retirement and the dental coverage selected by the annuitant. The primary government recognizes the cost of providing health and dental insurance to annuitants on a pay-as-you-go basis. The cost of these benefits for the year ended June 30, 2005, was approximately \$800 million.

Also, the University of California, a discretely presented component unit, provides to retired employees certain health plan benefits in addition to pension benefits. Employees who meet specific requirements may continue their medical and dental benefits into retirement and continue to receive University of California contributions for those benefits. There are approximately 39,600 retirees eligible to receive such benefits. The cost of retiree medical and dental coverage is recognized when paid. The cost of providing medical and dental benefits for retirees and their families and survivors for the year ended June 30, 2005, was \$193 million.

NOTE 25: SUBSEQUENT EVENTS

The following information describes significant events that occurred subsequent to June 30, 2005, but prior to the date of the auditor's report.

The primary government issued \$4.0 billion in general obligation bonds to retire previously issued commercial paper, to repay internal state loans, and to finance various school, prison, water, housing, library, transportation, and children's hospital projects. The primary government also issued revenue anticipation notes of \$3.0 billion that are due to be redeemed in June 2006.

The Regents of the University of California issued \$911 million in General Revenue Bonds to finance and refinance certain facilities and projects of the university. They also issued \$616 million in Limited Project Revenue Bonds to finance and refinance the acquisition, construction, renovation, and improvements of certain auxiliary enterprises of the university.

The California State University issued Systemwide Revenue Bonds in the amount of \$676 million for construction projects and to refund certain bonds including \$28 million in debt of the discretely presented auxiliary organizations.

The Department of Water Resources issued \$2.6 billion in Supply Power Revenue Bonds.

The California Infrastructure and Economic Development Bank issued State School Fund Apportionment Lease Revenue Bonds totaling \$97 million and Infrastructure State Revolving Fund Revenue Bonds totaling \$53 million.

The State Public Works Board, an agency whose activities are accounted for as an enterprise fund, issued lease revenue bonds totaling \$735 million for the benefit of the Regents of the University of California and various state agencies. Of the bond proceeds, \$470 million will be used to refund outstanding bonds.

The San Francisco State Building Authority and the Oakland State Building Authority, whose activities are accounted for as capital project funds, issued lease revenue bonds totaling \$201 million and \$28 million, respectively.

The Golden State Tobacco Securitization Corporation issued \$3.1 billion in Enhanced Tobacco Settlement Asset-Backed Bonds. Of the bond proceeds, \$2.6 billion will be used to refund outstanding bonds.

In July 2005, Fitch Ratings raised its rating on California's general obligation bonds from "A-" to "A" and Moody's Investor Service upgraded the State of California's general obligation bonds to A2 from A3.

